ESG: Going green & coming clean

Nordea On Your Mind
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IMPORTANT INFORMATION AND DISCLOSURES AT THE END OF THIS REPORT
SAVE THE DATE

The Nordic Sustainable Finance Conference
Friday 22 September 2017, Stockholm

We are proud to announce that Nordea will be hosting the first ‘Nordic Sustainable Finance Conference’ in Stockholm on Friday 22 September 2017.

The conference is targeting key business and financial leaders in the Nordic region and will address the growing focus on sustainability within the financial market.

The day will include presentations and discussions, with key topics such as:

- What is the relevance of sustainability in the context of finance and how can it be used to create positive value for shareholders and the society as a whole?
- Why should corporates and investors look to include sustainability considerations into their financial strategies?
- What are the major developments in the financial markets with regards to sustainability and how is it expected to grow in the future?

We look forward to seeing you in September where we will provide a unique opportunity to network with key stakeholders taking part in shaping the future of sustainability in finance.

Date: Friday September 22, 2017
Time: 10:00 – 15:00
Venue: Grand Hotel

Kind regards,
Nordea Corporate & Investment Banking

For registration and further information, please contact: carina.a.olsson@nordea.com
ESG: Going green and coming clean

Sustainability – Drivers shifting from ideological to commercial
ESG – environmental, social and corporate governance – has its historical roots in ideological movements and has, to a great extent, been about doing good (or at least being perceived to do good). We increasingly note a shift among both corporates and investors and a sharpening of focus on ESG, based on rising public opinion pressure to show good corporate citizenship and many examples in recent years of the costs – both to reputation and cash flow – of ESG incidents. Such – sometimes dramatic – costs need to be avoided, meaning ESG has to be taken very seriously.

Socially responsible investments (SRI) continue to gain ground – Europe leading the way
Total assets under management in SRI investment policies have seen a CAGR of 15% over the past four years, reaching USD ~23 trillion at the end of 2016. This represents 26% of global assets under management, up from 21% in 2012. Europe is at the forefront of applying SRI investment policies, at 53%, with the US and Asia lagging behind.

Green bonds coming of age
Historically, socially responsible investing has been about exclusion of "untouchable" securities. Focus is now shifting towards scoring and rating securities for ESG, selecting investments in strong performers. An instrument for positive differentiation is green bonds, first issued by the European Investment Bank in 2007, which fund specific green projects. Green bonds remain a niche market (0.7% of global bond issuance), but one that has seen a CAGR of 126% for 2010-16, surpassing EUR 200bn, and with more than 450 issuers across the entire credit spectrum as of early 2017.

ESG can be all about money: ESG-related costs for Nordic listed companies
As an illustration of a commercial driver for ambitious ESG adoption (seeing and trying to avoid similar ESG-related costs to those that others have suffered), we review 238 listed Nordic companies for ESG incidents in 2013-17. We note that 19% of the companies had ESG incidents, and 11% have had actual or expected costs for their incidents. Total costs of EUR 3.5bn correspond to 3% of annual EBIT for the full sample of 238, and 16% (!) of annual EBIT for the 19% actually affected.

What do the experts say? Views from EIB, Stora Enso, Tele2 and Nordea
In this issue of Nordea On Your Mind, we interview Bertrand de Mazières, Director General – Finance, and Eila Kreivi, Head of Capital Markets, at the European Investment Bank on how EIB became a pioneer for green bonds. On the corporate side, we interview Stora Enso’s CEO Karl-Henrik Sundström and Tele2’s CEO Allison Kirkby on how their respective companies have embedded ESG and sustainability into their respective business strategies. We also interview Nordea’s Head of Corporate & Investment Banking Mathias Leijon, and Head of Sustainable Finance Sasja Beslik on Nordea’s recently raised ambitions in ESG and sustainability.
Interview: The time for ESG is now

We interview Mathias Leijon, Head of Corporate and Investment Banking at Nordea on why ESG matters for both investors and corporates. In Nordea Asset Management, ESG has been applied successfully for years. Corporates are now starting to realise that sustainability is crucial not only for image and perception, but for actual, long-term operating and financial performance. Nordea wants to take a leadership position within ESG also outside Asset Management, to support our corporate customers, to pursue new business opportunities, but also to reduce risk in our own balance sheet.

KK: How would you describe the development of ESG and its key benefits?

ML: Concepts such as ESG (environmental, social and governance), CSR (corporate social responsibility) and SRI (socially responsible investments) emerged from ethical investments. The problem with the concept of ethical investments was that although the investor could sleep well at night with a clean conscience, the investment was most often a very poor one. It was expensive and it underperformed. What investors desire is an alternative where the soft parameters, such as ESG, match the hard ones, the financial parameters. In other words: an investment product that can be sustainable without sacrificing a good yield. Within the area of asset management we are already there, and Nordea is leading the way with its STAR concept. But for a corporate issuer of bonds or equity to be able to offer sustainable investment alternatives, it needs to accept some initial investments to achieve the key requirements. There will be costs for qualifying to be considered sustainable. These costs are long-term investments to create a more robust business model. Securing a strong ESG performance will, for a company, over time mean avoiding problems and incidents related to sustainability. This should ultimately create a competitive advantage, both by reducing – or even avoiding – ESG-related costs, and by reducing volatility in the cash flow generated from the absence of such major incidents. Over time, this should reduce the risk premium investors will apply to the company’s cost of capital.

KK: What do you think are the driving forces behind the initiative?

Increased awareness and demands among Nordea's customers?
Pressure from politicians, authorities and the public debate? A higher ambition from Nordea's board and management that the bank should be a role model in this area? Others?

ML: I would say the main driving forces are:

1. We will take responsibility in assisting our customers in their quest to become even better

2. From Nordea's perspective we will reduce the risk in our balance sheet over time

3. This is an area that creates a lot of pride both with our customers and our own staff

4. And finally, we contribute to something of greater good.
Most companies demand sustainable alternatives today as they know that being sustainable will create value, and that is why the timing for an ESG investment at Nordea is just right.

The reason we choose to make this investment now at Nordea is because we believe the timing is right. It is happening right now, and we have a chance to position ourselves as part of it and become no. 1 in this field. We also have a responsibility as the largest bank in the Nordics to help our customers. With the strongest Nordic DCM platform, highlighted recently by 12 different no. 1 positions in rankings by Dealogic, as well as the in-depth knowledge of ESG in Nordea’s asset management business, we could really accomplish lasting change. Just a few years ago there were still large companies who did not grasp the importance of ESG and there was a lot of confusion about what it really was. This included myself. Today, most corporates and investors want to be part of it. There is now widespread understanding among companies that this creates value, not least by avoiding value destruction. ESG is not an issue until it has become an issue. And when it has, it can be very costly indeed.

KK: Has the general perception of sustainable investments changed over time? Do you see a big difference among our customers and investors today compared with ten to 20 years ago?

ESG is about meeting our criteria, covering environmental protection, human rights, employee rights and anti-corruption.

ML: The big change did not happen that long ago; I would say it came three to five years ago. Before that, the general perception of sustainable finance, or ESG, was mostly a “do good” or charity mentality. But ESG is not about that. ESG is about investing in companies that meet our ESG criteria, covering environmental protection, human rights, employee rights and anti-corruption. The relative importance of the various criteria will vary by company. For a company where labour costs weigh heavily in the P&L, it might, for example, be particularly important to invest in education, corporate culture and healthy general working conditions. If the company does not, employee turnover will most likely be high, which could have significant negative consequences.

KK: Do you see sustainable finance mostly as a question of perception and image for the companies today? Or are there other, commercial, reasons, which drive the companies to work with these issues?

Previously, the main driving force for ESG related to image; today it has shifted to commercial aspects.

ML: Earlier, the incentive for driving ESG issues in companies related to image and perception. Today, I would say the focus has shifted to more commercial aspects. Companies have realised that it is a competitive advantage to engage in ESG. Another aspect is that demand for sustainable products and services, such as ecological products, has grown immensely. It would not have been possible 20 years ago to earn the same amount of money on ecological goods.

KK: Would you say Nordea has a particular responsibility to adopt and drive ESG, as the biggest bank in the Nordics? Should we act as a role model?

Nordea as a bank has a responsibility to drive the ESG development, but it's also a shared responsibility between us and our customers.

ML: Yes, of course we have a responsibility to drive this. In a way, we have already taken some responsibility, as I would argue Nordea Asset Management is the most competent and most experienced unit of its kind in the Nordics in this area of expertise. And we are making a major investment in this area right now. But I would also highlight that this is a shared responsibility between the bank and corporates; we cannot do this alone.
KK: What is the most important thing we can accomplish by offering sustainable products? Better returns on our customers’ investments? Being part of creating a better society? Strengthening the image of Nordea?

ML: All of these are important. To invest in sustainable assets gives a better risk-adjusted yield, which is beneficial both for the bank and customers. As a lender, we decrease the risk on our balance sheet, and the customer, the corporate issuer, gets a lower funding cost. Another important thing is that this kind of investment and commitment creates pride among our employees, which is of course positive.

KK: What kind of sustainable banking products will be offered in the future do you think? Today we have “green bonds” and investment funds that exclusively invest in securities that are compliant with ESG criteria. Can sustainability be a feature in more traditional banking products as well, such as loans and transaction services?

ML: We are currently looking at many different products across the business areas in the bank. A lot can be achieved by creating different hybrid instruments, but you have to test your way forward, see which ones will gain acceptance. Sustainability bonds are an example of such a product with at least one Nordic issuer in the market so far. The future will tell if sustainability bonds will develop further or if the interest among investors is too low. But the concept of sustainability is here to stay, and in general we have seen a major change of attitudes amongst customers. If there is real demand, I am sure we will aim to offer green loans in the future.

KK: You are already in a position where you can influence the work being done in this area at Nordea. But if you were given totally free reign to shape how Nordea should work with sustainable finances, would you do something differently, and why?

ML: I would do exactly what we are doing today. We have a great team of immensely talented and committed individuals and I feel we have great support for what we are doing. We are all excited about the opportunity to make a lasting difference.
ESG – An introduction

Sustainability, or environmental social and corporate governance (ESG), in running a business and investing in companies has its origins in ideological and religious movements, evolved with the emergence of civil rights movements, and has more recently been fuelled further by UN initiatives and environmental awareness. Lately, sustainability has seen a surge in momentum, with 53% of assets under management in Europe currently being run under socially responsible investment policies. Investors and corporates are recognising that sustainability is a must for value creation, or even survival.

Democratic leaders answer to their voters, corporate leaders answer to their owners – who typically wish to maximise financial performance

Leveraging capital to drive change
In modern, open societies, leaders answer to the electorate and can be removed from office if voters lose confidence in them, or disagree with their policies or how they are delivering on promises and commitments. Private corporations have leaders who answer to their owners. Corporations must abide by laws and regulations, and can certainly be greatly affected by public opinion on how they are behaving. However, their leaders follow the agenda of the owners, which is typically dominated by the aim to maximise the financial performance – and hence ultimately the value – of the business. Society sets the rules for what corporations can and cannot do. But these rules tend to outlaw more radical behaviour that is considered harmful to society. Regulations do not outline in detail how corporations should be run operationally or how management should go about seeking to maximise profit and cash flows.

ESG = Environmental, Social and corporate Governance

ESG is an acronym for Environmental, Social and corporate Governance, and is a set of standards for running a business that takes into account the company's conduct and impact on society in the environmental, social and governance areas.

Early incarnations of ESG include the Quaker movement and the founder of Methodism, who took stands against slave trade and harmful investments

ESG has been around for centuries, at least in more crude or narrow forms. A very early incarnation of ESG was the religious Quaker movement in North America, which in the mid-18th century prohibited its members from participating in the slave trade, more than 100 years before it was formally banned after the American civil war. Another early ESG proponent of the same era (18th century) was English cleric John Wesley, co-founder of Methodism, whose famous sermon "The Use of Money" urged investors not to harm their neighbours through harmful business practices, such as pollution from tanning and chemical production. He also preached that investors should stay clear of "sinful" companies like makers of arms, liquor and tobacco.

Money never stays with me. It would burn me if it did. I throw it out of my hands as soon as possible, lest it should find its way into my heart.

John Wesley (1703-1791)

From the 1950s, ESG was boosted by emerging civil rights movements

These ideas attracted more attention during the rapid development of civil rights movements in many developed countries in the 1950s, 60s and 70s. US trade unions started to make their pooled pension funds invest in socially beneficial projects for their members, like housing and medical facilities. Growing international opposition to the apartheid system in South Africa after the Sharpeville massacre in 1960, led to growing pressure on institutional investors (spearheaded by public, faith-based and pension institutions) to distance themselves from companies involved with the South African regime. The resulting plunge in foreign investment in the country eventually made South African companies start to call for the abolishment of apartheid, which contributed to its demise in 1994.
From the 1990s, climate awareness became a new, strong driver

In the 1990s, concerns about the environment and climate change became a new driver for focus on ESG. This has been further sustained by global UN-sponsored treaties such as the Kyoto Protocol of 1997 and the Paris Agreement of 2015.

The UN introduced six principles for responsible investment (PRI) in 2005, which now have ~1,600 signatories and over USD 62 trillion in assets under management

The UN has also contributed more directly to ESG through its then Secretary-General Kofi Annan bringing together an international network of investors to agree to commit to six principles for responsible investment (PRI) in 2005. The principles cover an array of possible actions to incorporate ESG issues in investments in all asset classes. They are voluntary and aspirational, but signatories are obliged to report to what extent they are implementing the principles in their annual reporting and assessment process. The principles were launched in 2006 and as of November 2016 had ~1,600 signatories in total, representing more than USD 62 trillion in assets under management.

The principles are as follows: As institutional investors, we have a duty to act in the best long-term interests of our beneficiaries. In this fiduciary role, we believe that environmental, social, and corporate governance (ESG) issues can affect the performance of investment portfolios (to varying degrees across companies, sectors, regions, asset classes and through time). We also recognise that applying these Principles may better align investors with broader objectives of society. Therefore, where consistent with our fiduciary responsibilities, we commit to the following:

1. We will incorporate ESG issues into investment analysis and decision-making processes.
2. We will be active owners and incorporate ESG issues into our ownership policies and practices.
3. We will seek appropriate disclosure on ESG issues by the entities in which we invest.
4. We will promote acceptance and implementation of the Principles within the investment industry.
5. We will work together to enhance our effectiveness in implementing the Principles.
6. We will each report on our activities and progress towards implementing the Principles.
Broadly speaking, we could describe ESG factors as being related to sustainability. It is all about aiming to run a sustainable business, one which can last and perform over time, both in terms of impact on society and own financial health.

Focus on ESG has gathered momentum and grown more strongly in recent years. This has been driven by political developments as well as focus in society and public opinion about sustainability issues. However, another critical driver has been a number of notable, high-profile ESG failures at large companies over the past ten years. These have highlighted how the financial impact from ESG issues for shareholders and creditors can be substantial, even dramatic. Five examples of such ESG-related issues are:

- **Turing Pharmaceuticals** acquired anti-parasitic drug Daraprim from Impax Laboratories in 2015, and raised the price more than 5,000% from USD 13.50 to USD 750 per pill. The combination of the drug being used by AIDS patients, and Turing’s young, ex-hedge fund manager CEO publicly rejecting all criticism of trying to make profit at the expense of highly vulnerable patients, gave the price hike massive public – including political – attention, some of which arguably made a mark on the US presidential election campaign in 2016.

- **BP** found itself responsible for the largest marine oil spill in history in 2010, when the Deepwater Horizon rig it leased from Transocean Drilling failed resulting in an explosion that killed 11 and injured 17. BP has estimated total costs for the incident at USD 61.6bn.

- **Lehman Brothers** was heavily exposed to US subprime mortgage lending, which ultimately led to its bankruptcy in 2008 – the largest in US history. Lehman had, partly through acquiring mortgage lenders, in effect become a real estate hedge fund in the shape of an investment bank. At the time of its bankruptcy, it had USD 22.5bn in capital with total assets of USD 680bn, meaning a 3-4% decline in asset value would wipe out its equity.

- **Rana Plaza** was an eight-storey commercial building in Dhaka, Bangladesh, used for garment manufacturing. It was owned by a businessman who ordered textile workers back to work despite the discovery of cracks in the building, which had four more floors added than were allowed in the original building permit. On 24 April 2013, the building collapsed, killing 1,129 people inside, and injuring another ~2,500. Several European and US clothing retailers were sourcing garments from the textile workshops in the building.

- **News Corp** caused a blow to confidence and trust in the publishing industry in 2006, when its UK newspaper News of the World saw its editor and a hired private investigator jailed for hacking into the private voicemails of celebrities. Further investigations showed in 2011 that questionable practices were more widespread, including accessing the mobile phone of a murdered schoolgirl as well as relatives of victims of the 7 July 2005 London bombings. This caused the eventual closure of News of the World, and made News Corp back away from an intended acquisition of UK TV broadcaster BSkyB.

Incidents such as these have helped raise investor awareness that business practices not compatible with sustainability can be value-destroying. This has heightened the focus on ESG, and shifted it from historically arguably more image and perception to more commercial – it is too costly to have ownership or credit exposure to companies that could suffer major financial blows from failure to comply with ESG standards.
Global assets under management under socially responsible investment policies have seen a CAGR of 15% in 2012-16

As an illustration of the increasing investor focus on ESG, data from The Forum for Sustainable and Responsible Investment (USSIF) shows that global assets under management under socially responsible investment policies have seen growth (CAGR) of 15% in just the past four years. The graph below clearly shows that Europe continues to lead the way with most global assets under management under SRI policies, but North America is catching up, and has grown three times as fast in the same period. Asia is lagging sharply, but growing fast from a low starting base.

26% of global assets under management are being run under SRI policies, up from 21% in 2012

For Europe, this figure is 53%

How significant have SRI schemes become in the context of the overall global asset management industry? Actually, they are a global force to be reckoned with, representing 26% of the world's assets under management. This is up from 21% four years ago. Here, Europe's lead shows even more clearly, with over half of European assets under management being run under SRI policies. The corresponding share for the US is 22%, and for Asia still less than 1%.

Investors and corporates are now adopting ESG for commercial reasons – incidents can be too costly

So, while in the past much ESG focus has had its roots in ideological beliefs, societies and public opinion have evolved to make it more urgent for corporations to be perceived as good corporate citizens in order to successfully conduct business. And we now see increasing evidence of the next – likely even more dynamic – phase in corporate and investor focus on ESG and sustainability: a shift from wishing to do good (or at least being seen to do good) towards recognising that not living up to high standards for sustainability can be very costly, or even potentially an...
existential threat. In other words, if a company is not run on a sustainable basis, there might not be a business to run in the future.

This has created several strong concrete drivers for increased focus on sustainability. Investors do not want to see their shares and bonds lose value from issuers suffering ESG incidents, and are demanding high sustainability standards from corporates they invest in. Corporates increasingly see and realise how painful costs from ESG incidents can be, and do not wish to suffer such costs, and subsequently be held accountable for them by their owners, and by society. And corporates increasingly see the long-term risks of being de-selected by investors who only wish to own stocks and bonds issued by entities with strong sustainability profiles. Funding could become a scarce resource for those who do not belong to this category, and valuations of issued securities could suffer, for those who risk ending up in a "structurally under-owned" category – consisting of securities the mainstream (and certainly the dedicated SRI) investment community does not wish to touch.
Interview: The responsible challenger

We interview Allison Kirkby, CEO of listed Nordic telecom operator Tele2, about sustainability and what it means for business. Since Allison became CEO in 2015, sustainability has become an intrinsic part of Tele2’s strategy, based on the belief that strong long-term returns to shareholders cannot be created unless they are created sustainably. Specific initiatives include annual commitments from staff to the corporate Code of Conduct, the appointment of a Group Privacy Officer, the banning of child sexual abuse images ahead of legislation, reduced energy consumption in networks, and a clear long-term bias in management pay.


AK: For Tele2, ESG – or our "Responsible Challenger" strategy – is absolutely part of our DNA. We have always been the customer champion, and I think the natural extension of that is being the society champion. I fundamentally believe corporations have a responsibility to the societies they operate in to make themselves sustainable for the long term. This fits very well with Tele2's core values of "open", "flexible" and "challenge". This is what we are all about. Hence, I believe you could include many of the aspects that you mention, but with an overweight towards a business opportunity.

JT: Tele2 decided in 2015 to incorporate Corporate Responsibility into the foundation of your group strategy, defining the company as a “Responsible Challenger”. What drove this decision?

AK: When I became CEO in 2015, I felt there had been some great CSR work carried out at Tele2, but at the same time I felt it was a bit strange that it was not an intrinsic part of our strategy. The risk was for it to be seen as a separate work stream, which would send the wrong message. It is a fundamental part of our strategy. We only create value for shareholders if we do it in a sustainable and responsible way.

JT: What would you see as the risks, or the downside, for the company, from not having a healthy ESG profile? Costs from fines or penalties? Availability of funding? The valuation of the company? Lost business opportunities?

AK: There is an abundance of data showing that companies which do not act in a responsible or a sustainable way perform considerably worse than those which are doing so. I strongly believe non-sustainability minded companies will underperform their peers in total shareholder returns. And you need to have sustainability embedded in your strategy. Just a PR programme will not be enough to avoid underperformance. You need to have employees who fundamentally believe that doing the right thing as a corporate is the right thing to do in every action they take. It starts from the bottom and works all the way up. It needs to be deeply embedded in the organisation. Without that, there is a far greater risk that something will go wrong.

JT: You make every one of Tele2’s ~6,800 employees, in all your markets worldwide, sign the company’s Code of Conduct annually. How come, and what does your Code of Conduct cover?
All employees do e-learning on Tele2’s Code of Conduct, and physically sign off on it

To ensure they don't forget about it, they get a refresher every year. We send them a reminder when a year has passed to take a new e-learning, and we check that they have done it. If they don't do it, it gets escalated up the management ladder, and ultimately comes to me. When I see someone has not completed the annual refresher, I send them a message saying "Oi!". It is amazing how quickly you get a reaction then!

Our board of directors have to come do it, too. And when we take on a new supplier, we make them commit to our Code of Conduct as well. There are examples of suppliers we have not taken on, when they refused.

The one exemption would be suppliers, typically the very large US corporates, who have their own established codes of conduct. We then test our code against theirs to make sure we have common values and ethical business practices

JT: You have a major business in Kazakhstan, which you actually expanded through an acquisition last year. A big competitor with a significant Eurasian business has seen irregularities in it lead to senior management departures and a public declaration of an intention to exit the region altogether. What are you doing differently, to ensure Tele2 does not suffer similar problems?

AK: We do not comment on what our peers are doing, but I am happy to describe our method. I think we have always had very strong ethics and compliance approaches. We did very deep due diligence before entering the market in Kazakhstan in 2010, as part of the M&A process at the time. When we entered, we quickly established the Tele2 values with the new organisation, with specific "The Tele2 Way" training, always involving our senior leadership. We aimed to make it very clear what is acceptable and what is not at Tele2, made everyone sign our Code of Conduct, and we have kept re-training them every year, like we do with all our staff. When we merged our Kazakhstani operation with Altel last year, we got a third party to audit our Code of Conduct and our approaches, and also help us with the training.

JT: You appointed a Group Privacy Officer in 2016. What was the reason for this, and what is the purpose of this role?

AK: We have a huge duty regarding privacy of the data that both our corporate and private customers entrust us with. With new regulations and legislation coming out, we felt it was necessary to appoint one senior individual to stay on top of this and ensure we adapt to it locally in each of the markets in which we operate. We wanted to signal that this is a priority for us, with a dedicated senior leader focusing on data security holistically, across our business. She is part of a working group, including our CFO, our Head of Security and people within our network and IT organisation to make sure we have a holistic view on these topics.

JT: Diversity is a core component in your “Responsible Challenger” status, and I could call Tele2 a role model in having a female CEO. Worldwide, you employ 40% women, and among your managers, 34% are women. Are you happy with that? If you see any need for
change, is it all up to the company, or would you need regulatory or legal reform to drive change?

AK: Even a Scottish female CEO – how about that? No, really, diversity for us is not only about gender, but means having a workforce which represents the demographics of the customers we serve. We will not be happy as a company until we do. I think we are doing a pretty good job on gender diversity, but diversity is for us much broader than just gender.

We have a subcommittee of our board for corporate responsibility, which evaluates our progress on gender diversity. I know our Swedish organisation is doing a lot in support of ethnic diversity, particularly in our stores and our customer service organisations, helping with language and cultural capabilities to be able to serve our customers well.

Do I believe in quotas and targets to drive diversity? No I don't. I fundamentally believe the best people for a job should be hired for it, irrespective of ethnicity or gender. I am, however, a strong supporter of governments and various bodies encouraging and supporting those groups less represented in the workforce to progress through the different ranks.

I would hate to think that I got a CEO role because the board wanted to tick the box of having a female CEO. I would have hated that throughout my career. I want women to get senior roles because they are the best qualified for them.

JT: How are children’s rights a relevant area for Tele2, and what are you doing about them?

AK: Child protection is a huge responsibility for us as a mobile operator. Our children increasingly live with these communication devices, and with open networks they can access anything. We were one of the first operators to block child sexual abuse images, across all of our markets, even including those markets where it was deemed illegal to do so. One example is the Netherlands, where until a year or two ago, it was illegal to block anything. At the time we took a stance, and blocked such images, despite our move actually being illegal. It was the right thing to do.

We also have a strategic partnership with Reach for Change, which helps social entrepreneurs develop innovations that create a better world for children. I sit on the board of Reach for Change, and Tele2 is one of their biggest sponsors.

All that said, there is more we can do in this area, not least in helping to educate children, to help them protect themselves.

JT: Is environmental protection an area where Tele2 can make any meaningful difference? If so, how?

AK: Telecoms naturally have a major impact on the environment, through reducing our need for travel and for sending documents in the post. But there is more we can do to have a positive impact on the environment. The tower of our networks consume energy, and we have launched a recent initiative to reduce energy consumption in our Swedish network, particularly our 4G network which makes up around 70% of our total energy consumption. I also believe the continued evolution of the internet-of-things (IoT), when machines increasingly communicate with each other, will allow monitoring and analysis of energy inefficiencies. Here our networks can be used to find inefficiencies and help further improve energy consumption.
JT: The “G” in ESG stands for governance, which includes management compensation and incentivisation. What is Tele2’s thinking regarding how to give incentives for top management to strike the right balance between long term and short term financial performance? Does ESG feature in any way in current management compensation?

AK: There is not a specific ESG metric in top management's performance targets, but our targets are very much aligned with what our shareholders expect of us. Our remuneration committee is trying to strike a balance between keeping management focused on long-term value creation and ensuring that compensation is competitive. They have over the past few years tried to shift more of management remuneration into long-term benefits, although there are caps in Sweden for how great that share can be. This year, there is even a share of management's short-term incentives which will be deferred, depending on value creation in certain business units in the group.

As a management team, we only want to get rewarded if the shareholders are getting rewarded as they have expected. Our in-year, short-term deliveries are very much linked to delivery on the long-term plan. And the long-term deliveries are heavily linked to total shareholder return and return on capital employed over a three-year period. We in the management have to invest ourselves to participate in the long-term incentives, so we are also shareholders. We currently have around 300 managers who are part of Tele2’s long-term incentive programme. These are the leadership teams of all the countries and group functions, and the next level down.
Interview: Not being sustainable is not an option

We interview Karl-Henrik Sundström, CEO of listed forest products group Stora Enso, on how the company’s view on sustainability has changed after having faced multiple ESG-related challenges. Heads of sustainability have been included in management teams for the business areas and the group, highlighting that it is not a separate function but rather a part of core values and strategy – and increasingly a major competitive advantage.

JT: Process industries are frequently in the spotlight for sustainability, facing obvious issues such as energy consumption, emissions and raw material usage. But Stora Enso at first glance appears quite sustainability-oriented: Your logo is a shining sun; you call yourselves "The renewable materials company"; you have a Head of Sustainability in the group management team; and you have a specific presentation for ESG (Environmental, Social and Governance) investors. You have been with Stora Enso since 2012, and CEO since 2014. How has the company’s view on ESG changed since you joined?

KHS: Stora Enso has worked actively with sustainability issues for a long time, but historically we have had a structure where there turned out to be differences between what we were saying and what we were doing. This led to our suffering several sustainability-related problems, most notably child labour issues in Pakistan. My background in the group is in running the Paper and Wood Products business areas, which only have operations in the Nordic region and Austria. Even if I was fortunate not to face ESG issues, customer behaviour showed me very clearly how a strong sustainability profile is a genuine competitive advantage. Customers care about our behaviour and that of our supply chains. Hence, when I became CEO in 2014, I immediately introduced a Head of Sustainability that reports directly to me in the group management team, and corresponding sustainability heads in the management team for each of our divisions.

We discovered how any ESG issue affects the brand of the entire group. We had to face municipal customers with zero tolerance policies for labour law issues, which is a real problem if you happen to be Sweden’s biggest supplier of biofuels. And it didn't matter if the problems had arisen in another part of the group, indeed in another part of the world.

On day #2 in my new job as CEO, I visited our tree plantation in Beihai in China together with then Finnish Minister for Ownership Steering Pekka Haavisto. It was important to show, and to hear confirmed, that we were doing the right things to set things straight regarding land ownership issues. It was a running start.

JT: What has driven the focus Stora Enso has on sustainability today? Demands from regulators and authorities? Desire for a strong brand and image? Demands from owners and investors? Demands from customers? Own experiences from setbacks or challenges?

KHS: We have responded to sustainability signals from all stakeholders: owners, employees, customers, suppliers. And we have wanted to change our mindset, from following rules to establishing a competitive advantage in order to become a sustainability role model.
JT: You are within an industry undergoing tremendous change: paper was 70% of your revenues 10 years ago and has halved to 33% today; the Biomaterials business area did not exist in 2006 but is 14% of revenues today. Has this been a driver for Stora Enso to see sustainability and ESG as not only compliance with regulations, but also a cornerstone of your corporate strategy?

KHS: It has definitely been a driver. I would point to seven megatrends in the world today that are greatly affecting us:

1. Growing population
2. Urbanisation
3. Digitalisation
4. Growing middle class in developing economies
5. Global warming/climate change
6. Changing lifestyles (the sharing economy, eating out more, etc.)
7. Increasing sustainability awareness (making sustainable consumption choices)

In our industry, we are very fortunate in having a raw material that is renewable and can be recycled. Trees grow. Swedish forests have grown 40% since World War II, despite increased harvesting. Wood fibre is a great sustainable resource, and in the future you will be able to use it to make all products that are today made from fossil-based materials.

We have accordingly tried to shift our focus from paper to the new growth areas, which include wood products for construction, packaging and pulp/biochemicals.

These may seem like moderate changes in our business mix in the past 10 years, but they need to be seen in the context of installed paper machines in our factories typically having a service life of 50-70 years. For us, the changes have been radical. And this is partly why we are so keen to pursue sustainability as a competitive advantage. We need it, in this fast-changing world.

JT: Stora Enso has faced several ESG-related challenges in the past few years – how has this affected the company?

KHS: We had to forcefully address our challenges head-on, to restore our credibility and brand. We had some unhappy customers, some unhappy suppliers, several major investors who did not want to own our shares, employees who felt ashamed of their employer...my own mother called me to ask what we were doing!

We have tried to make use of our challenges to introduce a genuine and ambitious sustainability agenda into the company, and to embrace it not just because we have to, but to build a competitive advantage because it makes business sense to do so. I think it is no coincidence that many companies that have a strong sustainability profile have suffered problems in this field in the past. We are no exception. We even have some customers who say they don't want to engage in any deeper sustainability dialogue with suppliers who have not suffered some sort of sustainability-related crisis. We note that many peers have sustainability as an area of responsibility under communications, while we have it included in our commercial, business area and management activities.
JT: Do you see any differences in behaviour, or in the dialogue you have with equity and bond investors today, compared with when you joined Stora Enso? Are there benefits from being seen as sustainable? Or any disadvantages from not being seen as a strong performer within ESG?

KHS: Back then we had a much more defensive posture, as we had to respond to questions and concerns on ESG issues. When would problems be resolved, and what would it cost? Today, we are proactive and transparent in highlighting all we are doing within sustainability, and we are no longer getting those concerned questions. I have in this period met all dedicated sustainability investors in the Nordic region more than once, and I can see very clearly that we have improved from how we used to be perceived.

Benefits from having a strong ESG profile are obvious regarding being considered an acceptable supplier by large municipal customers and global brand owners and from having access to institutional investors with stringent ESG criteria in capital markets.

JT: You have a Supplier Code of Conduct for your suppliers. What do you ask of them? Do you expect your supplier base to change going forward? If this happens, will you be able to stay competitive?

KHS: We ask them to sign a document in which they commit to our sustainability principles after an extensive risk-based review. We audit them fairly frequently, but those who have signed are pre-qualified to deliver to us. This year, we have expanded our Code of Conduct to include safety. Historically, our industry has seen a couple of fatal accidents per year, often in transports. We would like to eliminate that, together with our suppliers.

We have some 20,000 suppliers today. We look for them to share our view on sustainability in addition to being innovative, quality-oriented and compliant with labour laws. So far, suppliers accounting for 95% of our annual purchase value have signed up to our Code of Conduct. And yes, we have ended relationships with suppliers who would not.

Our profitability has increased since we introduced our supplier Code of Conduct. I don't see any threat to competitiveness from our using it. On the contrary, I think doing the right thing will clearly prove to be the most commercially successful strategy. Doing the wrong thing is what proves to be most costly, when problems arise. That is what can make you uncompetitive.

JT: How are you affected by changing customer behaviour? Do you see growing demand for sustainable products? Are customers prepared to pay a premium for them? Are you seeing banning or limitations for non-sustainable products?

KHS: It varies. For some products, customers are prepared to pay a premium if it is sustainable. For other products, sustainability is a hygiene factor. Customer will not consider buying it at all, unless it is considered to be sustainable. This often applies to high-margin products.

Stora Enso is quite unique in having 90% of our wood material certified. In Europe, only 10% of forests are FSC (Forest Stewardship Council) certified, and we manage a great share of that 10%.
JT: Stora Enso has done much to show its focus on sustainability, not least through initiatives to address ESG challenges you have faced. Are there any financial or other incentives for management to deliver on all the company's ambitions within ESG? If there are not, should there be any?

KHS: To me, sticking to our ESG principles and policies is the core of who we are and how we work. I see it as a prerequisite, something I expect from everyone at Stora Enso. I don't think it would make sense to reward staying true to our values – do what is right – with some sort of bonus. I would say not doing it is simply not an option. Compare when you have received your driving licence: You are then allowed to drive a car. Does that mean you should get a reward for actually stopping at the red light?

JT: As seen from the outside, Stora Enso seems to have suffered most ESG-related challenges in developing markets. Are there any regrets regarding your major expansion in these markets, which started in earnest 10-15 years ago?

KHS: We certainly don't regret our expansion in the developing markets. It was necessary in order to re-shape the company to match where our markets were heading. But we could have been even better prepared when expanding in these markets.

Earlier in my career I worked for telecom equipment maker Ericsson, which had been active in virtually every far away market in the world for up to 100 years. Ericsson knew these markets inside and out, while for the paper and forest industry, these regions were new.

But I think choosing an easy way out, simply opting not to be present in these new markets, means denying the shareholders growth opportunities. New markets should not be avoided just because they are difficult to operate in, but thorough homework needs to be done before entering them, to prepare for the challenges that lie ahead and minimise risks from them.

Look at our expansion into China as an example. We had two major cartonboard mills, one in Sweden and one in Finland, whose output has been virtually sold out for years. Market growth is coming from Asia. When new capacity needed to be added, it was an obvious choice for us to add it in China.
Green funding: Green bonds coming of age

Green bonds are bonds whose proceeds are earmarked to fund specific green projects, and such use is validated and subsequently reported. The first green bond in the world was issued in 2007, by the European Investment Bank (EIB). The green bond market has grown rapidly since, surpassing EUR 200bn in early 2017, with over 450 private and public issuers, across the entire credit spectrum. Issuance really took off from 2014, when China entered the market, with additional impetus from Poland and France issuing the first ever sovereign green bonds (in France's case a 22-year EUR 7bn bond!) three to four months ago.

Investors have historically applied ESG through exclusion, by not investing in "bad" industries or companies

Historically, application of ESG, usually through socially responsible investment (SRI) approaches, from investors' point of view has been on the basis of exclusion. Investors have opted not to offer funding (buy shares or bonds) to corporates which do not live up to the investors' criteria for sustainability. This has started to shift towards an application based on inclusion. Investors are evaluating the sustainability performance of issuers, and deciding on which issuers qualify for investing in, and which do not. This in theory allows investors to apply different risk premiums, and hence different required rates of return, to different issuers. And these risk premiums can be – significantly – influenced by performance or score for sustainability criteria.

Taking this a step further, issuers can seek positive differentiation. We could call it inclusion. Issuers who have a particularly strong sustainability profile could seek funding from investors who require just that. Or issuers who have specific sustainability-oriented projects which need funding could turn to sustainability-minded investors for financing of these.

Green bonds premiered in 2007, the first issued by EIB

Ten years ago, in 2007, we saw the birth of such a (positively) differentiated investment instrument: the green bond. It was pioneered by the European Investment Bank (see our interview with the EIB's Director General – Finance and Head of Capital Markets in this report), which issued the world's first green bond.

A green bond is essentially an ordinary bond, whose proceeds will be used for environmental-oriented investments. There is still very little formal legislation or regulations for green bonds, but a market standard has emerged over the past ten years, co-ordinated through the International Capital Market Association. The ICMA has established a set of Green Bond Principles, which are a framework for defining and classifying green bonds. The principles have four core components:

1. Use of Proceeds
2. Process for Project Evaluation and Selection
3. Management of Proceeds
4. Reporting

This means the principles are to be used to ensure that any green bond will be used exclusively to fund environmental or sustainability projects, and that proceeds are earmarked and tracked, with subsequent reporting by the issuer on their use in the projects. However, the project assets are not pledged as collateral, and so the credit risk of the bond is backed by the whole cash flow of the issuer.
The principles include a recommendation that an issuer uses an external review to confirm the alignment of their green bonds with the key features of the Green Bond Principles. Such a review represents a second opinion.

Compared with the size of the global bond market, green bonds remain a small niche. But green bond issuance has grown tremendously since 2010, showing a CAGR of 126% between 2010 and 2016 (measured in EUR of issuance). This compares with a CAGR of a mere 2% for ordinary bonds. In annual volume terms, the green bond market has grown from less than EUR 1bn in 2007 to over EUR 75bn in 2016, with annualised volumes in 2017 year-to-date pointing towards a potentially even higher number for 2017.

Green bonds remain a small niche, but global issuance has seen CAGR of 126% since 2010

Green bond issuance CAGR 120% in the Nordic region in 2010-16

In the Nordic region, the development has been similar to that seen on the global level, although even slightly more polarised. Ordinary bond issuance has seen a CAGR of just under 1% in 2010-16, while green bond issuance has seen a CAGR of 120%.

Source: Dealogic and Climate Bonds Initiative
In 2016, green bonds were 1.7% of total issuance in the Nordics, versus 0.7% globally.

This leads to a striking observation, which we try to illustrate more clearly in the graph below: green bonds represent a higher share of total bond issuance in the Nordic region than in the rest of the world. In the past three years, the difference has become even more pronounced. The overall share of green bonds is still quite small compared with total bond issuance, but the share in the Nordic region is 3-4x the level of the global average. In 2016, green bonds accounted for 1.7% of total issuance in the Nordic region versus 0.7% globally.

Global green bond issuance has surged since 2014

Global green bond issuance took off in terms of absolute volumes in 2014, and last year it more than doubled even from that level. Ultra-low interest rates have buoyed bond markets generally, but as we saw above, growth for green bonds has vastly outperformed the overall market. Rising investor appetites for sustainable investment instruments, strong political and public opinion drivers, and maturing market practices and standards for green bonds have all helped. In other words, despite highly favourable market conditions for ordinary bond funding, green bonds have continued to dramatically outgrow ordinary bond issuance, underscoring how strong the drivers for seeking green funding have been.

The Nordic region has on average represented 5% of global green bond issuance

The Nordic region has in the past eight years represented 2%-10% of annual green bond issuance, with an average of 5%. Against this backdrop, it is fair to say that the Nordic region punches above its weight in adoption of green bonds, considering the size of its economies.
Looking at the mix of currencies green bonds have been issued in, we see a strong dominance of USD and EUR, which is quite natural given the large sizes of the global bond markets in these currencies. At the same time, we can see CNY coming in third place, highlighting China’s recent entry into the green bond market, coming in with a bang. And the Nordic region’s embracing of green bonds is further illustrated by SEK being the fourth largest currency for such bonds to date. We note the absence of JPY in the current stock of green bonds, which illustrates how the rest of Asia is lagging the global development in the green bond market.

Among specific green bond issuers for aggregated volumes in 2007-16, EIB is no. 1 by a good margin, with 9% of total issuance to date. It is followed by four issuers with 4%-5% each, where a notable newcomer is the Republic of France. This year has seen the entry of sovereigns in the green bond market. Given the size of typical sovereign issuance, this could be a major growth driver for the green bond market going forward.
Total global green bond issuance has now exceeded EUR 200bn, with over 450 issuers, spread across the credit spectrum.

From being a marginal phenomenon when it was created through the EIB issuing the world's first green bond in 2007, the global green bond market has surpassed EUR 200bn in aggregated issuance in Q1 2017. The green bond universe now includes over 450 issuers, across the entire credit spectrum, from non-rated to AAA-rated. It now includes virtually all types of issuers:

- **Sovereigns** (eg France, Poland)
- **Banks** (eg China Industrial Bank Co, Bank of China, Bank of America, Unibail-Rodamco)
- **Regional and local government** (eg Region Île de France, New York Metropolitan Transportation Authority, Province of Ontario)
- **Utilities** (eg Electricité de France, GDF Suez, Iberdrola, Southern Power Co, Mexico City Airport Trust, State Grid Corp of China)
- **Multilateral/Agency** (eg EIB, KFW, the World Bank, the Nordic Investment Bank, Asian Development Bank)
- **Manufacturers** (eg Toyota, Apple)
- **Real Estate** (eg Vasakronan)

The biggest development in the green bond market in 2016 was China, which dominated the market with some EUR 30bn of new issuance during the year. This represented one-third of total global issuance, and two-thirds of growth over 2015. About half of China's green bond issuers to date are banks, which represent three-quarters of China's total issuance. China's surge has been propelled by the central bank (PBOC) publishing Chinese green bond standards and quotas in December 2015.

Another major development last year was the first entry of a sovereign issuer in the green bond market. Poland issued a EUR 750m five-year note to fund renewable energy, clean transport, sustainable agriculture and conservation in December 2016. It was a high-profile move, for a country with 90% of its electricity output from coal-fired power generation.

France followed Poland's lead with quite a splash, issuing a 22-year EUR 7bn green bond in January 2017. This is the biggest green bond issue in the world to date.

From the very beginning ten years ago, green bonds were not introduced with any specific ambition to achieve better pricing (lower funding cost) than ordinary bonds. They were an instrument allowing the borrower to show a green, sustainable, profile and ambition. And they were meant to secure an issuer access to the growing investor base managing money...
under socially responsible investment policies. This has allowed green bond issuers to tap into a new investor base, and could – given the growth in the share of funds under management falling under SRI policies – gradually turn into a more "defensive" strategy: ensuring that the issuer retains access to mainstream funding sources. We could easily envisage a not-too-distant future, in which the threshold (in SRI/sustainability terms) for being considered "investable" could be raised substantially. Big issuers in bond markets may not be able to afford not having access to the SRI investor base.
Interview: EIB, creator of the green bond market

We interview Bertrand de Mazières, Director General – Finance, and Eila Kreivi, Head of Capital Markets, at the European Investment Bank, exploring the EIB’s mission and mandate, how the institution pioneered the concept of green bonds ten years ago and how it became the world’s biggest issuer of green bonds to date.

JT: How would you very briefly describe the EIB’s mission and mandate today? Has it changed significantly in recent years, and has it changed much from what the EIB was at its formation back in 1958?

BdM: The mandate of the bank has actually not changed since its creation. The EIB is meant to help fund long-term investment in Europe, what economists would call fixed capital formation. But the context of long-term funding needs has certainly changed from 60 years ago. Back then there was a heavy emphasis on regional funding support for poorer regions in southern Europe – the EIB has even on occasion been referred to as “the bank for the Mezzogiorno”. This was of course an exaggeration, as its scope has never been limited to southern Italy. But there was a strong theme of boosting investment in lagging regions, to bring a more even level across Europe.

Today, themes have become much more varied, major ones for the EIB being

- Environmental protection and climate action
- Support for SMEs (small and medium-sized enterprises)
- Support for research & development

The core of our mission remains to provide long-term financing for projects which are economically and financially viable, and sustainable. And we never fund projects on our own, we always co-finance with others.

JT: The EIB is a non-profit organisation. Does this affect how you evaluate projects you are invited to fund? How do you weigh sustainability merits of a project against commercial terms and risks?

BdM: Being a non-profit entity does not affect how we evaluate projects, in that they need to be economically and financially viable. Our non-profit nature shows in the funding cost we charge to our borrowers. Our price covers our own funding cost, plus a margin surcharge to cover project risks, but no additional margin for us to generate a profit. As such project risks have largely not materialised into any credit losses, we have in the past few years accumulated profits of some EUR 2.5bn per annum. But this should be seen as a build-up of reserves for future project risks.

On sustainability merits of projects, we see them as a component of financial viability. Projects need to be sustainable in order for us to consider them economically viable.

EK: As an example, when we consider the sustainability merits of a renewable energy project we are asked to co-finance, we do not take into account today's carbon fuel prices, but instead our assumed future carbon prices. This helps make such projects more attractive than they would appear under a static current-state analysis.
JT: Would you say that the EIB’s priorities and sustainability requirements for projects to be funded hold you back in how much business you would like to do? Are your criteria difficult to meet for project applicants?

BdM: Globally, no. I would say that here in Europe, a large share of projects naturally generated by the economy are already consistent with our sustainability criteria. More of a constraint for us is that investments in Europe remain subdued since the outbreak of the global financial crisis, and are even today below the level of 2008. So lack of origination is more of a constraint than our criteria.

We are well aware that having the EIB as a co-funder can make project discussions more complex – we can be seen by some as something of a difficult counterparty. But at the same time, our involvement gives projects a stamp of quality. We tend to be the party that sets the standard that every other party is happy to see applied – especially in project finance.

We do have some exclusion criteria, although not many. Coal-fired power generation is one. The production of armaments is another.

EK: Outside Europe, in developing economies, almost every large project is financed by several multilaterals. And they all have fairly similar evaluation criteria. Such borrowers are well familiar with what is expected from them in order for their projects to get funding.

JT: In the past 10 years, EIB has been the world’s biggest issuer of green bonds, accounting for 9% of issue volumes. This is more than twice as much as the global no. 2. Has EIB been a pioneer within green funding and green bonds? What have been the drivers behind the EIB’s prominent position as a green bond issuer – what are your success factors?

BdM: We were the first issuer of green bonds when we started in 2007. Given our mission, with funding environmental investments as a priority area, we were a quite natural issuer of these instruments, and our premiere was in the same year that the EU introduced its first common environmental policy with climate targets.

Right from the start, we wanted to do as much as possible to establish a market for green bonds, so we issued in several currencies, and in several tenors, to establish a yield curve for the bonds.

Will we remain the biggest in the future? I really doubt it, because now, in 2017, we have seen sovereigns entering the green bond market. France issued EUR 7bn in a single bond! And we are quite happy to see these new entrants drive further development of this market.

EK: We were ambitious, and put in place a pretty rigorous process for the issuing of green bonds from the beginning. We introduced the concept of separating the funds from green bond proceeds, earmarking them for specific sustainability projects. We listed the criteria for projects to qualify, and required reporting of how funds received from bond issue were actually used. This is all still in use today, although it has been developed and refined further.

Green bonds were initially mostly a retail investor market, but really took off to become a major institutional market as well from 2013. This has partly been driven by climate protection evolving from a purely political agenda into also being a financial markets agenda, helped by global initiatives like the UN-sponsored Paris Agreement of 2015.
Since 2013, we have also been very involved in the International Capital Market Association’s (ICMA) Green Bond Principles (GBP), and I currently chair the GBP’s Executive Committee.

JT: Does the EIB fund itself exclusively in capital markets? How big a share of your capital markets funding is green bonds? Where do you see this share in five years? In your 2017-19 operational plan, you see a funding need of EUR 15bn for the period. Could the EIB’s size be a constraint to finding required funding?

Our share of green bonds is less than 10% of total and most likely we will see some kind of stabilisation around this level. The level of green bond issuance is closely linked to our lending portfolio.

BdM: Yes, we fund ourselves exclusively in the capital markets. The only exception is our own capital, paid by the EU member states. This capital is also invested in our loan portfolio. In 2013, the member states increased our capital, paying in an additional EUR 10bn and hence doubling our capital base.

In the past couple of years we have issued the equivalent of some EUR 2bn in green bonds, out of a total programme of EUR 60-65bn, so the share of green bonds is less than 10%. We don’t have any target for the green bond share of our funding, but I think it would be reasonable to expect some kind of stabilisation not too far from current levels.

EK: The level of green bond issuance should be quite closely linked to our lending portfolio. We have dedicated our green bonds to two of our project sectors: renewable energy and energy efficiency. Any expansion of our green bond funding would most naturally come from adding additional sectors, like – for example – transport. But this would require that those sectors can meet requirements for verification of qualifying for sustainability criteria, and defining metrics for impact reporting. We are looking into possibilities to add more sectors, but I would not expect any major, big, new ones to be added in the near future.

JT: How do you perceive green bonds compared with ordinary bonds? Are there differences in pricing? Differences in access to investors who are prepared and able to invest in each type of bond? Changes in regulations or market practices? Is the situation very different today, compared with five years ago, or ten years ago?

On the primary market there is no price difference between green and ordinary bonds but we’ve seen that green bonds have been somewhat more expensive on the secondary market. That could indicate an undersupply of green bonds.

BdM: Before issuing our first green bond in 2007, we expected it to be priced like ordinary bonds. This has also happened, and has continued since. We have more recently seen some examples of green bonds being priced with somewhat tighter spreads (priced more highly) in the secondary market, compared with ordinary bonds from the same issuers. This could indicate a certain scarcity value for green bonds, since the supply of green bonds is more limited.

While we did not aim for better pricing of our green bonds, I think we have been successful in our aim to both broaden and deepen our bond investor base by being able to offer both green and ordinary bonds.

EK: Generally, in the green bond market, we have seen that first-time issuers have entered the market offering just a small or even no first issuer premium to investors. Also, long tenors have been more easily accessible than with ordinary bonds. There has been a lasting excess demand for green bonds in the market.

Compared to ten years ago there has been a sea change in rules and regulations regarding green bonds – from nothing to the GBP being standard-setter today.

BdM: There has been a sea change in rules and regulations, from nothing 10 years ago, to the GBP being a standard-setter today. This is industry standards, agreed by 120 members and 80 observers, including investors, issuers, underwriters and rating agencies. But some formal regulations are now coming. In France, for instance, investors are now required by law to...
disclose what they are doing regarding climate change, in response to the country’s energy transition for the future. China is introducing government-defined criteria for what qualifies as green investments. The G20 have assigned a study group for environmental finance co-chaired by the Bank of England and China to establish some agreed G20 policy lines. And the central banks of China and the EIB are doing a joint study of green investment criteria to evaluate how the national Chinese ones match the international agreed standards.

While the green bond market has grown and evolved in the past 10 years, there has been a lingering fear of an “accident”, that there would be an instance of cheating or shortcomings on the part of an issuer. Thankfully, this has so far not happened. And the market is of such a size and sophistication today, that I believe an incident like that would no longer be an existential threat to the market.

JT: Do you see major differences between countries in how investors view green bonds? Any countries which stand out? If so, what do you think has made them stand out, in embracing or rejecting green bonds?

EK: Some countries have been more early adopters of green bonds, like Sweden and the Netherlands. France has been quite early as well. China is joining this group, too. Asia is generally lagging. The US is more patchy, with some real global trendsetter investors, and some who are not getting involved at all.

JT: The green bond market is still a relatively new phenomenon; do you see any shortcomings or flaws in how the green or sustainability categorisation is carried out by third parties? Is the process too costly or complicated? Does it measure the right things? How could it be improved?

EK: I think there is a need for streamlining and standardisation of third parties’ verifying that green bonds satisfy sustainability criteria. Today the scope of the verification varies greatly, from a one-page summary criteria check list for a bond, to a 30-page evaluation of the sustainability profile of the issuer. I think verifiers could benefit greatly from establishing some best practices for their offering. Members of the Green Bond Principles will respect that they have varying business models and agendas, but will argue that it would give universal benefit if transparency and efficiency in the verification process were improved.

We know cost for verification to qualify for sustainability can be an issue, particularly for small to medium-sized issuers who wish to enter the green bond market. Spending perhaps 20,000-30,000 EUR needs to be justified. A standard template for verification could reduce the cost, or at least potentially allow issuers to choose a cheaper “light” version if it suffices for their needs, instead of paying for a full 30-page report.

BdM: Actually, Singapore is introducing a state subsidy for the verification cost, to incentivise issuers to enter the green bond market. In general, I think any issuer will need to see the cost as an investment, made to ensure access to as big a bond investor base as possible, and to strengthen one’s own brand and image. We are also seeing examples of new green bond issuers also reviewing the asset side of their balance sheet, how they invest and what they invest in. And this is really what green bonds are about, making issuers aware of sustainability issues, and wanting to stay proactively on top of them.
JT: How do you think the EIB’s mandate and mission will evolve in the next 5-10 years? You are planning to increase own resources lending from EUR 71bn to EUR 76bn by 2019. Will that be enough, given all that is happening in Europe’s neighbouring areas? Could the EIB do more?

BdM: You can infer from current ongoing discussions within the EU that the EIB’s mandate should be more of the same. There should be a continuation of "The Juncker Plan" (for investments in Europe) into the "The Juncker Plan II", which the EIB will support. The EIB should retain its mandate of up to some 10% of its lending outside the EU.

Regarding future lending volumes, don’t forget the multiplier effect: behind each euro of EIB financing, there is normally two or three euros of co-financing. We are a financial institution, so regulations will put a limit to how much we could expand lending with maintained leverage ratios and other key metrics. But our funding as an anchor should be able to meet a lot of the needs we may see in Europe and its vicinity in the next few years.
ESG: It can be all about the money

While ESG has historically come from a desire to do good, we have seen corporates and investors sharpen their focus in recent years owing to evidence of how painful ESG incidents can be – both for reputation and financial performance. To illustrate why and how this has become so relevant – for commercial rather than ideological reasons – we review 238 Nordic listed companies. In the past five years, 19% of them have had ESG incidents, and 11% have had ESG-related costs. These costs correspond to 3% of EBIT for the whole universe, and 16% (!) of EBIT for the affected companies.

ESG was originally about a desire to do good, and the image that goes with it
As we have discussed earlier in this report, the origins of ESG came from ideological and religious beliefs, and movements arising out of those. Early specific issues such as slavery and pollution have seen the addition of environmental, civil, human and labour rights issues, giving sustainability, ESG and socially responsible investing (SRI) a broader scope today. But one main reason for adopting ESG over the years has been a desire to do good. Companies championing ESG strive to be seen as good corporate citizens, looking at a greater good beyond short-term cash flows. Investors with SRI policies have sought to establish an image as guardians of precious capital, only putting it to use in companies whose behaviour render them worthy of receiving it.

Nordic companies and investors are focusing more and more on ESG – for financial reasons
This is all well and good. But we sense that the general perception among corporates and investors regarding ESG is changing. What we pick up – particularly among companies who have suffered (or nearly suffered) ESG-related problems – is a tendency to make a strong statement, and establish a culture, for wanting to do the right thing. And this desire for an "automatic" drive to always do what is right, comes from a strong belief that doing the wrong things (suffer ESG-related incidents) can be extremely costly – not only for image and brand, but certainly in real money. It can cause major negative cash flows. It can even cause the death of a business, with a massive loss of value for shareholders and lenders.

Corporates want to avoid ESG incidents because they can be costly
So, corporates seem to be increasingly adopting ESG practices, re-defining how they run their business, in order to ensure that they avoid suffering ESG-related incidents. They do not just want to be perceived to be doing the right thing, ie not breaking any rules. They want to avoid costs, to reputation as well as in the form of charges or cash outflows, for not having conducted their businesses in a sustainable manner.

Investors want to avoid ESG incidents because they can damage investment portfolio performance
Investors are doing the same, particularly in the Nordic region. They want to avoid including stocks and bonds in their investment portfolios that could see major downside, or even see their value wiped out, from ESG incidents. One or a few such blow-ups could put a serious dent in monthly, quarterly or even yearly performance, relative to whatever index the fund manager is benchmarked and evaluated against.

Public opinion has been a driver of increased ESG focus, and watching ESG incidents and associated costs for other companies even more so
What is driving this focus on ESG, this determination to avoid value destruction from ESG-related problems? Public opinion has surely had an impact. The emergence of political populism in developed countries in the past few years has made "misbehaving" corporates more likely to become targets of public discontent. This could come in the form of penalties, regulation, legal action or customers distancing themselves from the company, hurting demand. But a critical factor for the increased focus has been witnessing ESG incidents, and how they have affected the companies involved.

In the introduction section of this report, we mention some examples of high-profile, significant ESG failures at international companies. Here, we
To indicate the impact of ESG incidents in 2013-17, we have reviewed 238 Nordic companies covered by Nordea Equity Research. We review a sample of 238 listed Nordic companies, from all four Nordic countries (Sweden, Denmark, Norway and Finland), which Nordea Equity Research covers. We asked our equity analysts covering these companies to highlight any ESG-related issues each company has suffered in the past five years (2013-17), what the issues have been, and what costs, if any, were associated with the issues. Through this exercise, we wish to give an insight into how common and how serious ESG incidents are (or at least have been) in the large corporate sector in the Nordic region.

Our review does not portray the whole picture, but gives a general idea. As ever, methodology can always be discussed. We have no ambition to present the whole picture in this review. We merely want to provide a general overview of the magnitude of ESG-related problems in the Nordic countries, and we argue our analysis is useful for that.

19% of companies have had ESG incidents. First, we want to have a rough look at the frequency of significant ESG-related problems in this universe of companies. We note that out of the 238 Nordic listed companies, 19% have had some form of ESG incident on at least one occasion in the past five years.

We have a broad definition of ESG issues, including tax processes. We opt for a broad definition of ESG here, for example including tax issues, where authorities initiate investigations into companies for tax evasion. This does not need to mean any deliberate criminal activity on the part of the company, and can simply be driven by a changed agenda for the tax authorities. Nonetheless, we include such issues under ESG, when the amounts involved have been well beyond typical fluctuations in taxation relating to ongoing operations.

11% of companies have had actual or expected ESG-related costs. We also note that 11% of the 238 companies have in the past five years had actual, specified costs for ESG-related issues. This means more than one in ten, in a five-year period. In other words, there have arguably been a fair number of eye-openers for what ESG setbacks can mean for business, readily observable by other companies.

Total ESG-related costs in 2013-17 are EUR ~3.5bn. And what about those actual costs, then? Aggregated five-year average annual EBIT for the full sample of 238 companies is EUR ~109bn. The corresponding EBIT for 19% of those companies who have had ESG incidents is EUR ~22bn, and the specific ESG-related costs (according to the companies – and this includes cash expenditure and reservations/assumptions) are in aggregate EUR ~3.5bn.

Share of Nordic listed companies with ESG issues and costs, 2013-17

And what about those actual costs, then? Aggregated five-year average annual EBIT for the full sample of 238 companies is EUR ~109bn. The corresponding EBIT for 19% of those companies who have had ESG incidents is EUR ~22bn, and the specific ESG-related costs (according to the companies – and this includes cash expenditure and reservations/assumptions) are in aggregate EUR ~3.5bn.
ESG-related costs represent 16% of EBIT for affected companies, 3% of EBIT for all 238 companies.

Putting it another way, ESG-related costs for the past five years correspond to 3% of annual EBIT for the total universe of companies, and 16% of EBIT for the sample of companies who have actually suffered ESG incidents. Look at that figure again: 16% of EBIT for those affected. For nearly all of those companies, this would wipe out more than a year's profit. For many, it would wipe out five years' profit. For some, it would wipe out ten years' profit. Hardly a coincidence that Nordic large corporates have sharpened their ESG focus in recent years.

![EBIT and costs for ESG issue for listed Nordic companies, 2013-17](image)

Source: Company data and Nordea Markets

We include a table reviewing those of the 238 companies that have suffered ESG incidents.

Below we include a full review of the 238 companies in our studied sample. We describe what ESG-related incidents they have experienced, what any estimated or actual costs related to it are, and each company’s market cap and five-year annual average EBIT, all translated into EUR. We also show the cost as a percentage of annual average EBIT.

Companies are ranked by ESG-related costs as a share of EBIT.

We then rank the companies according to how big a share of EBIT the costs they have suffered are. It is important to highlight that we are not in any way passing any judgement on any company here, nor are we trying to measure the quality of the companies in this exercise. Our purpose with this review is to give an overview of ESG-related issues in the past five years, and their order of magnitude in some kind of context.

We are not judging any companies, or trying to measure them on ESG.

As an example, Coloplast tops the list below by having provisions for product liabilities corresponding to 167% of annualised average EBIT. Coloplast’s issues originate from an acquired business in the US, they are legacy issues for which Coloplast could hardly be blamed. But the size of the related provisions puts Coloplast at the top of the list. This is simply an illustration of how product liability issues in the US can be quite costly.

It could be argued whether or not we should include all incidents below as ESG-related...

Again, it could be debated whether tax evasion processes should be considered ESG issues. The same could be argued for project management failures (there are some big project-related losses for the construction companies) and perhaps other problems in the list below as well. But at the same time, companies such as Telia and Ericsson potentially face major fines for ongoing corruption investigations, which could be of such a magnitude (proposed fine of SEK 12.5bn for Telia) that they would even change the percentages of annualised EBIT for our full sample of 238 companies. Both Ericsson and Telia are included in the review below at zero cost, since they have made no provisions, and given no own estimates of likely fines.

...but there also some big issues which have no specified cost yet, which would likely bring up the total cost significantly – the net should give a good overall indication.
## Cost of ESG failures, 2013-17*

<table>
<thead>
<tr>
<th>Company</th>
<th>Market Cap EURm*</th>
<th>ESG Issue</th>
<th>ESG Cost**</th>
<th>Cost/ EBIT</th>
<th>Other</th>
<th>Cost EURm</th>
<th>EBIT EURm***</th>
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<tbody>
<tr>
<td>Coloplast</td>
<td>14,769</td>
<td>Coloplast has faced lawsuits over its vaginal mesh products since 2012. All competitors have been involved in similar cases.</td>
<td>167% Coloplast has provisioned DKK 5.25bn for settlements.</td>
<td></td>
<td>Coloplast is very highly regarded for its ESG profile and consistently ranks among the top companies in relevant ESG/CSR rankings.</td>
<td>704</td>
<td>422</td>
</tr>
<tr>
<td>Kungsleden</td>
<td>1,194</td>
<td>Convicted of tax evasion.</td>
<td>139% SEK ~3000m</td>
<td></td>
<td>The amount has been split on several occasions: 2015/2014/2012 (320+1350+1284)</td>
<td>331</td>
<td>237</td>
</tr>
<tr>
<td>Wilh. Wilhelmsen ASA</td>
<td>1,889</td>
<td>The whole industry is being investigated by antitrust authorities worldwide (since 2012).</td>
<td>119% WWASA has paid fines totalling USD 88m and made an additional provision of USD 143m.</td>
<td></td>
<td></td>
<td>217</td>
<td>183</td>
</tr>
<tr>
<td>Peab</td>
<td>2,439</td>
<td>Cost overrun issue: Mall of Scandinavia and Tele2.</td>
<td>79% SEK 800m, SEK 300m</td>
<td></td>
<td>The amount has been split on several occasions: 2015 and 2012 (800+300)</td>
<td>120</td>
<td>153</td>
</tr>
<tr>
<td>SAS</td>
<td>883</td>
<td>In March 2017, the European Commission re-adopted a cartel decision against 11 airlines for operating a price-fixing cartel. A judgement was passed already in 2010 but was later appealed by SAS.</td>
<td>52% Almost EUR 800m divided between the 11 companies.</td>
<td></td>
<td></td>
<td>70</td>
<td>136</td>
</tr>
<tr>
<td>G4S</td>
<td>5,517</td>
<td>Convicted for overcharging tens of millions of pounds on electronic tagging contracts for offenders (2013).</td>
<td>48% GBP 109m</td>
<td></td>
<td>In 2015, G4S lost a contract to run the Rainsbrook secure training centre for young offenders due to poor staff behaviour.</td>
<td>128</td>
<td>265</td>
</tr>
<tr>
<td>Fabege</td>
<td>2,589</td>
<td>Convicted of tax evasion.</td>
<td>47% SEK 1,900m</td>
<td></td>
<td></td>
<td>220</td>
<td>467</td>
</tr>
<tr>
<td>SKF</td>
<td>8,163</td>
<td>In 2014, the European Commission fined six companies for operating a price-fixing cartel in the market for automotive bearings.</td>
<td>43% The Commission imposed fines totalling EUR 953m.</td>
<td></td>
<td></td>
<td>315</td>
<td>733</td>
</tr>
<tr>
<td>Volvo</td>
<td>27,756</td>
<td>Several truck makers were accused of operating as a cartel over a 14-year period (1997-2011).</td>
<td>41% Volvo fined in 2016: EUR 670m</td>
<td></td>
<td></td>
<td>670</td>
<td>1,636</td>
</tr>
</tbody>
</table>

*Continues on next five pages.
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<tr>
<td>SCA</td>
<td>21,062</td>
<td>After the corruption scandal in 2014, both the chairman of the board (Sverker-Martin-Löf) and the CEO (Jan Johanson) resigned. The attention from media mostly related to reports on misuse of the company's jets and exclusive hunting trips. Even the company's auditors, PwC, faced scrutiny for taking part in the trips. According to AR2016, the company has reserved SEK 1,300 m for ongoing tax cases in Sweden and Austria. SCA has also reserved SEK 1,090m for ongoing antitrust cases in Chile, Colombia, Poland, Spain and Hungary.</td>
<td>Johansson received severance pay of two years' salary: SEK 22m. Tax reservations: SEK 1,300m+ SEK 1,090m</td>
<td>24%</td>
<td></td>
<td>253</td>
<td>1,051</td>
</tr>
<tr>
<td>NCC</td>
<td>2,547</td>
<td>Write-downs on current project in Norway. In 2015, NCC paid a fine for cartel activity in 2005-08 (Asphalt cartel). NCC has appealed the judgement.</td>
<td>Write-downs: SEK 350m (2016); Fine: SEK 143m (2015)</td>
<td>19%</td>
<td></td>
<td>52</td>
<td>273</td>
</tr>
<tr>
<td>Getinge</td>
<td>3,649</td>
<td>The FDA inspected a number of Medical Systems' manufacturing units in 2013, which led to observations about the facilities' quality management system. In 2015, a US court approved an agreement (Consent Decree) between Medical Systems and the FDA.</td>
<td>The total financial consequences related to the Consent Decree in 2015 amounted to approximately SEK 500m, excluding the remediation programme.</td>
<td>16%</td>
<td></td>
<td>53</td>
<td>343</td>
</tr>
<tr>
<td>GN Store Nord</td>
<td>3,146</td>
<td>In 2015, GN discovered fraud in its Beltone retail franchise network.</td>
<td>GN took a DKK 150m one-off loss for the inflated numbers.</td>
<td>14%</td>
<td></td>
<td>20</td>
<td>148</td>
</tr>
<tr>
<td>Huhtamaki</td>
<td>3,484</td>
<td>Huhtamaki received a fine from the European Commission in 2015 for its role in a pricing cartel operating in France and north-western Europe. The company also had some disputes with labour unions in the US in 2014. The unions claimed that Huhtamaki has tried to prevent its workers from organising at its plants.</td>
<td>EUR 15.5m</td>
<td>8%</td>
<td></td>
<td>16</td>
<td>191</td>
</tr>
<tr>
<td>Autoliv</td>
<td>8,014</td>
<td>Antitrust activity; price fixing on more than 30 types of car parts.</td>
<td>Autoliv paid USD 65m (2014) in a multi-district civil litigation to customers and car trades, etc. In 2015, DoJ handed down its judgement and a fine of USD 14.5m.</td>
<td>8%</td>
<td></td>
<td>49</td>
<td>618</td>
</tr>
<tr>
<td>NKT Holding</td>
<td>1,810</td>
<td>European cable producers were fined due to price cartel involvement.</td>
<td>NKT received a fine of EUR 4m.</td>
<td>7%</td>
<td></td>
<td>4</td>
<td>55</td>
</tr>
<tr>
<td>TGS Nopec</td>
<td>2,048</td>
<td>Fined in 2017 for tax cheating in 2009. The news broke in May 2014 and TGS has contested the claims.</td>
<td>NOK 85m</td>
<td>6%</td>
<td></td>
<td>9</td>
<td>171</td>
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<tr>
<td>Loomis</td>
<td>2,271</td>
<td>Loomis’ Spanish subsidiary has been under investigation by the Spanish competition authority (CNMC).</td>
<td>EUR 7m</td>
<td>5%</td>
<td>Loomis has appealed the decision in the Spanish courts.</td>
<td>7</td>
<td>149</td>
</tr>
<tr>
<td>DNB</td>
<td>23,648</td>
<td>In 2013, DNB was found guilty of “Røeggen Saken” which involved the mis-selling of index-linked bonds. There is currently an ongoing mass lawsuit against DNB for marketing of disguised index funds.</td>
<td>DNB took a NOK 450m charge for “Røeggen Saken” in Q1 2013 to compensate clients.</td>
<td>2%</td>
<td>DNB has not admitted any guilt in the ongoing lawsuit.</td>
<td>58</td>
<td>2,899</td>
</tr>
<tr>
<td>Yara International</td>
<td>9,901</td>
<td>Fined for bribing officials in India and Libya - including to the family of former Libyan leader Muammar Gaddafi's oil minister and the family of a financial adviser in India's Ministry of Chemicals and Fertilizers.</td>
<td>USD 36m</td>
<td>2%</td>
<td></td>
<td>32</td>
<td>1,347</td>
</tr>
<tr>
<td>Industrivärden</td>
<td>9,169</td>
<td>Anders Nyrén was dismissed as CEO after his involvement in the SCA scandal which involved private jet trips and hunting outings.</td>
<td>Nyrén received severance pay of two years’ salary; SEK 32.6m</td>
<td>0%</td>
<td></td>
<td>3</td>
<td>1,109</td>
</tr>
<tr>
<td>Nordea Bank</td>
<td>42,453</td>
<td>Fined by the FSA in 2015 and 2013 for breaking money laundering rules.</td>
<td>SEK 50m + SEK 30m</td>
<td>0%</td>
<td></td>
<td>9</td>
<td>4,358</td>
</tr>
<tr>
<td>Svenska Handelsbanken</td>
<td>24,042</td>
<td>Fined by the FSA in 2015 for breaking money laundering rules.</td>
<td>SEK 35m</td>
<td>0%</td>
<td></td>
<td>4</td>
<td>2,109</td>
</tr>
<tr>
<td>Telia Company</td>
<td>16,092</td>
<td>Uzbekistan corruption scandal.</td>
<td>Proposed fine of SEK 12.5bn.</td>
<td>0%</td>
<td></td>
<td>1</td>
<td>2,472</td>
</tr>
<tr>
<td>Aker ASA</td>
<td>2,768</td>
<td>Fined for insider trading in AKSO. Incident happened in April 2013 but first came out in 2014.</td>
<td>USD 8.5m</td>
<td>-7%</td>
<td></td>
<td>6</td>
<td>-94</td>
</tr>
<tr>
<td>Hennes &amp; Mauritz</td>
<td>33,058</td>
<td>Over the years H&amp;M has been accused of child labour and poor working conditions, but has not been fined so far.</td>
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<td></td>
<td>2,657</td>
</tr>
<tr>
<td>A.P. Møller - Mærsk</td>
<td>31,508</td>
<td>Ship breaking on Alang beach – environmental impact.</td>
<td>No cost to date.</td>
<td></td>
<td></td>
<td></td>
<td>2,916</td>
</tr>
<tr>
<td>Telenor</td>
<td>23,026</td>
<td>Vimpelcom was convicted of the same crime as Telia and the CFO of Telenor had to leave his position due to his involvement in the Vimpelcom scandal. This has indirectly influenced Telenor negatively.</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>2,273</td>
</tr>
<tr>
<td>Ericsson</td>
<td>19,745</td>
<td>Investigated by US authorities (SEC/DoJ) on suspicions of corruption.</td>
<td></td>
<td></td>
<td></td>
<td>1,621</td>
<td></td>
</tr>
<tr>
<td>Vestas Wind Systems</td>
<td>16,821</td>
<td>In 2014, several managers in Spain were fired. The specific reasons were not disclosed but fraud was a part of it.</td>
<td>No cost impact.</td>
<td></td>
<td></td>
<td>470</td>
<td></td>
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<tr>
<td>Norsk Hydro</td>
<td>11,157</td>
<td>Norsk Hydro is being investigated by the Norwegian Parliament regarding dealings with a Tajikistan aluminium plant. Tajikistan is considered to be among the most corrupt countries in the world</td>
<td>No cost to date.</td>
<td></td>
<td></td>
<td>529</td>
<td></td>
</tr>
<tr>
<td>Wärtsilä</td>
<td>10,217</td>
<td>Since last year (2016), the company is dealing with a case regarding fraud with the test results of its engines. Of the total of sold Wärtsilä engines, two percent were affected.</td>
<td>The scandal did not have a major financial or customer impact.</td>
<td></td>
<td></td>
<td>531</td>
<td></td>
</tr>
<tr>
<td>StoraEnso</td>
<td>8,886</td>
<td>The use of child labour in the sourcing of recycled fibre in Pakistan for the 35%-owned equity-accounted minority investment in Bulleh Shah Packaging remains a challenge, which is being addressed by supplier auditing, awareness-raising and support for local schooling.</td>
<td>The financial direct costs have been small (&lt; EUR 1m) or difficult to estimate. Combating irregularities is part of the company’s sustainability strategy which translates into 13 sustainability KPIs.</td>
<td></td>
<td></td>
<td>602</td>
<td></td>
</tr>
<tr>
<td>Nokian Tyres</td>
<td>5,141</td>
<td>Press reports in Finland revealed in February 2016 that Nokian had “cheated” in magazine tyre tests by sending different kinds of tyres to the test centres than those actually sold.</td>
<td>The issue caused a share price dip but did not really have any visible financial impact on the company.</td>
<td></td>
<td></td>
<td>343</td>
<td></td>
</tr>
<tr>
<td>Millicom</td>
<td>4,746</td>
<td>Guatemala corruption issue.</td>
<td>No cost to date.</td>
<td></td>
<td></td>
<td>708</td>
<td></td>
</tr>
<tr>
<td>Elekta</td>
<td>3,327</td>
<td>In 2015, Italian authorities initiated an investigation into some employees of Elekta’s Italian operations for suspected antitrust violations.</td>
<td>No cost to date.</td>
<td></td>
<td></td>
<td>143</td>
<td></td>
</tr>
<tr>
<td>Nets</td>
<td>3,078</td>
<td>The company had a big leakage of personal data in 2014 that enabled a celebrity magazine to track the credit card habits of Danish celebrities. It has also been under media scrutiny due to a generous management incentive programme that came into effect in connection with the IPO last year.</td>
<td></td>
<td></td>
<td></td>
<td>93</td>
<td></td>
</tr>
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<tr>
<td>AAK</td>
<td>2,657</td>
<td>Potential carcinogenic substances found in the company’s palm oil as a result of deodorisation.</td>
<td></td>
<td></td>
<td>No direct cost, but potential long-term negative effects stemming from customers opting for palm oil alternatives.</td>
<td>140</td>
<td></td>
</tr>
<tr>
<td>JM</td>
<td>2,340</td>
<td>Arbitration is ongoing on KKV8 (Fortum’s thermal pain in Stockholm). No write-downs yet.</td>
<td></td>
<td></td>
<td></td>
<td>181</td>
<td></td>
</tr>
<tr>
<td>Nobia</td>
<td>1,709</td>
<td>The company has had problems with one of its kitchen brands HTH. Some customers reported that their kitchen cabinets had fallen down (5 reports on a series out of 100,000-plus). The company offered to replace the cabinets for all affected customers.</td>
<td>If all of the customers would have complained about their cabinets, the company would have incurred costs of about SEK 50m. In the end, very few made a claim and the cost for the company was insignificant.</td>
<td></td>
<td>80</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Betsson</td>
<td>982</td>
<td>Betsson has been accused of corruption and money laundering in Georgia.</td>
<td></td>
<td></td>
<td></td>
<td>84</td>
<td></td>
</tr>
<tr>
<td>Eltel</td>
<td>370</td>
<td>Investigations on potential fraudulent accounting practises after the PE owner sold all shares in conjunction with the IPO in 2015. Subsequently, the CEO left the company in 2016.</td>
<td></td>
<td></td>
<td>Since the IPO in 2015, the stock is down from around SEK 100 to about SEK 53.</td>
<td>14</td>
<td></td>
</tr>
<tr>
<td>HKScan</td>
<td>164</td>
<td>HKScan terminated employment contracts with several members in its Baltic division’s management group in December 2016 after discovering they had been purchasing goods/services for HKScan from companies managed by the management members themselves or related parties.</td>
<td></td>
<td></td>
<td></td>
<td>26</td>
<td></td>
</tr>
<tr>
<td>Fortum</td>
<td>11,370</td>
<td></td>
<td></td>
<td></td>
<td>For ethical reasons, some investors do not put up money for companies operating in nuclear power and some investors want to exclude companies that have a 30%-plus coal-related business. For Fortum, however, only 8.2% of the energy it produces comes from coal.</td>
<td>1,030</td>
<td></td>
</tr>
<tr>
<td>Neste</td>
<td>9,500</td>
<td></td>
<td></td>
<td></td>
<td>Greenpeace claims that Neste destroys rain forests by using palm oil but the company claims that it uses only RSPO-certified palm oil. Neste’s earnings have not been affected by this dent in its reputation; in fact, the share price has actually risen over 600% when using palm oil.</td>
<td>591</td>
<td></td>
</tr>
</tbody>
</table>

*Market cap as of 19 April 2017 **Estimated ESG cost over the past five years, 2013-17 ***Average EBIT 2012-16

Source: Company data and Nordea Markets
Interview: Nordea is going clean

We interview Sasja Beslik, Head of Sustainable Finance at Nordea, about the work and increased focus within sustainable finance and sustainability at Nordea. Why has the initiative been taken now? Was it prompted by retail investors, politicians or something else? What difference can Nordea make, and do we have a responsibility to act? Sasja describes the development in the field over the recent years and why we are facing a breakthrough now.

For someone who doesn’t work directly with sustainability, it may be difficult to understand the difference between the concepts 'corporate social responsibility' and 'sustainable finance'. How would you distinguish them? Have they changed over time?

SB: If we start with 'corporate social responsibility', also known as CSR (corporate social responsibility), it began to take shape during the 1970s. During the Ronald Reagan and Margaret Thatcher administrations, a wave of deregulation shrank the public sectors in the US and the UK. As the private sector started representing a greater share of the economy, expectations grew for companies to take more responsibility for the impact they had on society. At first, this was called 'Corporate Citizenship' and later became CSR. Today, the concept is often just called CR (corporate responsibility). CR is a wide concept and at Nordea we call it 'sustainability'.

By definition, sustainability, or CR, applies to every way in which a company affects society through its operations. It can be anything from how it interacts with suppliers and employees, to the amount of paper or energy it consumes. In Nordea's case, sustainability is about corporate responsibility and issues related to the bank.

Sustainable Finance at Nordea determines issues that are related to customers, products and offerings in the fields of investments, lending and advice; hence we integrate sustainability into our work. Within Asset Management, we have a dedicated responsible investment team working with ESG issues for Nordea's funds.

Responsible investment, or ethical investment, started in Sweden and the Netherlands in the late 1980s, driven by the retail investor market.

Responsible investment as a concept emerged as a sub-category within CSR in the late 1980s. It started in Scandinavia, especially in Sweden, and in the Netherlands. From the beginning, it was based on ethics – how could financial capital be used in an ethical manner? The reason it started in Sweden and the Netherlands was the demands that had arisen from the retail investor market, which was much more mature regarding ethical investments than in other countries. In an ethical analysis, all companies that do not meet the predefined ethical standards are removed from the portfolio. This is also called 'negative screening'. At the time, ethical investments were criticised for being more expensive than alternative investments and also for underperforming. Just as the word 'social' had a negative connotation in CSR, the word 'ethics' had a negative connotation in ethical investments, as it was associated more with, for instance, religion.

During the 2000s, the analysis for responsible investment was modified and people started to talk about 'sustainable finance' rather than 'ethical investments'.

After 2000, there was a big change. First, people started to talk about 'sustainable finance' rather than 'ethical investment', but above all, the analysis was modified. Instead of excluding companies defined as 'bad', the new approach allowed people to invest in any company they liked as long as all investments were based on a few critical criteria. Not only was the potential return to be considered, but also environmental, social and governance aspects (ESG). Hence, put simply, the largest difference
between the ethical and the ESG analysis is that the former entails all the 'bad' companies being removed, while the latter means only investing in 'good' companies that are performing at an acceptable ESG standard.

At Nordea, we offer both ethical and ESG investments purely because some of our customers request ethical alternatives, especially certain institutions and foundations which are forced to make such investments in order to comply with their investment policies. I would happily only work with ESG investments, though.

KK: In 2016, Nordea made major changes within the sustainability area, indicating management and the board's wish to invest in sustainability. A new unit within Wealth Management was created, Sustainable Finance, headed by you, and a new Chief of Group Sustainability, Erik Feldt, was appointed in 2017. What will these changes accomplish?

SB: At Nordea, everything has to do with sustainability started within Asset Management, in the unit within Wealth Management that I mentioned earlier. I have worked with ESG issues at Nordea since I started here in 2009. In recent years, management has seen the need to integrate sustainability into all business areas and solutions. In 2016, the sustainability area was split into two: Sustainable Finance (headed by me) and Group Sustainability (headed by Erik Feldt). The latter group works with CR within Nordea, and addresses issues related to the bank, such as how we treat our employees and our suppliers, and what our energy consumption level is, etc. This group establishes policies on how we should act (code of conduct).

Sustainable Finance, the unit I am responsible for, determines issues that are related to customers and the business side. As I was explaining earlier, it is all about sustainability being integrated into the products and offerings in the fields of investments, lending and advice. This applies to all our business areas: Markets, Corporate & Investment Banking (C&IB), Commercial & Business Banking (C&BB), etc.

KK: What do you think are the driving forces behind the initiative? Increased awareness and demand among Nordea's customers? Pressure from politicians, authorities and the public debate? A higher ambition from Nordea's board and management that the bank should be a role model in this area? Something else?

SB: Primarily demand from customers. They have, for example, become more conscious about the fact that they can make a difference by actively choosing how to invest their money. Many of us have made conscious choices about the way we live our lives in order to make the world a better place. Somebody may choose to become a vegetarian, another to recycle cans and a third to use public transportation instead of buying a car. These are all examples of good, symbolic actions. But if these people go to their banks and invest all their savings in non-ethical/ESG alternatives, and if they then compare that amount of money with the amount of money they actually manage to save for society from being 'good citizens'…well, then the outcome is quite poor. People have finally started to realise this, and that is a big change.

Also, it is not impossible to imagine that there could be legislation in this area, meaning banks must show that they take responsibility for sustainability. This would apply to all their products.
KK: Despite the recent changes within sustainability at Nordea, do you think that we can work even more on sustainability in the bank? Do you see anything that we can improve on or do differently?

SB: One of the biggest challenges, which has become even more obvious now that we are establishing sustainability throughout the whole organisation, is that every unit except for Asset Management has some work to do within this field. They are lagging by almost five years. Hence we have to raise the pace and create new structures so that we can quickly get everybody on board. So far, some competitors have been better at embracing and implementing new products. One example is green bonds. I presented a proposal on how we could work with green bonds at Nordea in 2011. At that point, other banks hardly knew what green bonds were. Today, everybody associates green bonds in the Swedish market with SEB. We should focus on providing green alternatives throughout our total range of products. We can gain a lot if we take market shares in new, sustainable products: those that can create their own market have a great advantage!

Another thing that we can improve is communication. We do many great things at Nordea, but the outside world may never have heard of them. Since I started at the bank in 2009, I have frequently been in the media and I have participated in many different forums, but I still meet people at Nordea who have no idea who I am.

KK: Has the general perception of sustainable investments changed over time? Is there any area within sustainable investment that has become more or less important over the last ten to 20 years?

SB: A major change in this area is the attitude among fund managers and investors towards ESG; they have become much more positive. In the past three years, they have begun to realise that ESG investments actually provide better returns, by reducing risk. Take BP and Volkswagen as examples. With help from our ESG analysis, we can often see if there is an obvious risk of an ESG-related incident in these companies, although if there is, we cannot be certain when it will happen. That kind of analysis can help us save a lot of money. We (Nordea Asset Management) actually sold our equity stake in BP before its big accident in 2010. The reason for our decision was that we had estimated that the probability of this kind of event happening had increased significantly during the preceding few years. In our analysis, we looked in particular at the development of the company’s health and safety budget in relation to its expansion of exploration. To us, it was a clear warning signal when we saw that its safety budget began to fall despite the expansion.

We also work differently with sustainable finance today compared with previously. It could described as being based on three pillars. The first is an old-school approach, ‘negative screening’, which I described earlier. The second pillar is the ESG analysis, in which we look at our ESG parameters in order to choose which companies to invest in. The final pillar is trying to cooperate with companies that do not meet our ESG requirements. If we see a potential investment opportunity in a company, we gladly help it to fulfil our criteria so that we can be a part of its business. Thus, we reduce the risk in our investment and, at the same time, we make it cheaper for the company to access funding as its risk decreases. Hence, it is really a win-win situation. Our task is not to deselect companies; our task is to invest in companies. But it is also important to show integrity and to act when we think that a company has done something wrong. We did so when we sold our stakes in Telia Company and Stora Enso. We even got rid of our position in Nordea when the investigation into facilitation of tax evasion via Panama came to light. That was perhaps the only positive thing that was published in the media about Nordea and the Panama
affair. We stated that we disapproved of the situation that made an inquiry necessary, but it also showed that we are a big bank, and that while we might not all be the 'good guys', not all of us are necessarily the 'bad guys' either. And we stood by the interests of our investor customers.

I would also say that there has been a change in attitudes towards sustainability among listed companies. Companies have become much more transparent and better at reporting what they do within the ESG field, which facilitates our analysis a lot. Previously, it was much harder for us to make these analyses, and especially to compare the companies with each other. So we are seeing many positive changes within the area, which is, of course, very welcome.

**KK: Do you believe that Nordea has a particular responsibility to drive this, given that we are the largest bank in the Nordics – should we act as a role model?**

SB: Yes, we definitely have a responsibility to act as a role model. We are a global systemically important bank and we are a major player in the European banking industry. Additionally, mistakes within this field cost an enormous amount of money and, more importantly, lead to a loss of customer confidence. For instance, since our poor handling of compliance with money-laundering regulations was discovered, the number of man hours spent by the bank in this area has increased dramatically. That costs a large amount of money. But to lose customers' confidence is even more serious, as it takes so long to regain their trust and cannot be fixed during a round of golf or a customer event. Hence, it is important to show that we are a good role model, not only by – for instance – donating money to UNICEF, but also by offering sustainable products and helping companies to work with sustainability.

**KK: Is it possible for Nordea to make a real difference? Can you give an example of when we have done that?**

SB: Oh, there are plenty of examples! We can really make big changes that affect a great number of people. One example that I remember and that I'm quite proud of is that we have probably improved water conditions for hundreds of millions of people in India. We were involved in water management in pharmaceutical production in two Indian states. I was part of this project, about two years ago, and it made an impression on me. I even had to spend 48 hours in an Indian jail during the project!

**KK: What are you most proud of having accomplished since you joined Nordea?**

SB: What makes me most proud is that we are having this conversation today. Right now. Here. Three years ago, I cannot see how we would have ended up at this table together. As I mentioned earlier, we have worked with this for several years within Asset Management, and we have received a large number of prizes and awards, confirming that we have done a good job. But the fact that a new unit has been created within investments, lending and advice, integrating sustainable finance within the whole group, is a huge step and a great opportunity. I am very happy and excited about our new mission.
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