Sustainable Finance

Chapter 6

Valorisation

The true value of academic research does not derive solely from producing innovative ideas, using high-quality data, or from a researcher's skills to conduct a systematic investigation into the research question. These are merely the prerequisites for generating good research. For it to be truly valuable to our society and to have an impact, research must be communicated to the relevant audience in a practically suitable manner. This chapter summarizes the results and implications of the research findings with some useful suggestions on practical applications.

This thesis provides evidence on the value of sustainability information in the context of capital markets. Altogether, we find that sustainability matters to capital market participants and there is still ample room to integrate sustainability information into the decision-making procedures. Therefore, advancing research in this field is particularly beneficial and important, as it is still a largely unexplored domain, that promises great potential. The research in this book reveals the importance and potential influence of different stakeholders within the economy on driving sustainability, e.g. banks that channel large amounts of capital to certain projects or causes can play a critical role in promoting sustainability. If they refuse to lend or offer higher loan rates to borrowers that exhibit unsustainable practices this will impact how corporations operate and to what extent they integrate sustainability in their business thinking, regardless of the reason banks care and whether it is because they expect a different credit risk or whether they are protecting their own reputation. The findings in this book provide empirical evidence to all types of stakeholders that advancing in sustainability matters is possible without sacrificing financial benefits. It provides explicit information and evidence on particular cases in the debt and equity market in which sustainability (be it in terms of ESG performance, only governance, or non-financial disclosures) on potential mechanisms which can be employed in a practical setting. The next paragraphs explain in more detail the practical implications drawn from the individual chapters and briefly summarize only the main points of the main chapters, to put the practical conclusions into a more convenient context.

Chapter 2 assesses the relationship between top executive gender and the loan spreads of the respective company. In a broad sense, this chapter reveals that the debt market reflects whether the firm is run by a male or female top executives. By doing so, it provides useful evidence on the debate on whether the characteristics of the top executive matter at all. However, it shows even more than that: Using a cross-country sample allows us to identify whether differences in loan spreads are driven by internal corporate factors, or by society's attitude towards women in leadership positions. In terms of internal corporate factors, we account for executive-specific features, such as education, experience, age, and nationality in addition to loan, company, and economic characteristics, which may be driving loan spreads. In terms of external factors, we introduce cultural perceptions of female top executive skills as a new determinant in the loan pricing literature. Our results reveal that firms with female top executives receive better loan conditions than companies with male top executives, when cultural attitudes are progressive towards female executives. Otherwise, they receive worse loan conditions. The findings of this study indicate that having a female top executive is beneficial and companies may be able to reduce financing costs by strategically promoting female executives in countries with progressive attitudes, while companies may be better off with male executives in less progressive countries. Banks that are aware of this bias should look into their lending policies to detect whether they may be able to increase their competitiveness by offering more competitive loan spreads to companies run by female executives in countries with skeptical views on female top executive behavior in particular. Institutional and private investors can use this information to identify firms with lower debt costs, and hence higher cash flows to equity holders. They may also assert their influence on the firm to seek more favorable loan conditions based on the knowledge of this study. Regulators should find these results valuable in developing policies to improve gender equality. The results indicate that gender quotas may be insufficient in improving equality and economic welfare if they are not accompanied with the appropriate openness and acceptance. The full advantages of gender diversity can only be reached, when societal values support the integration of women in leadership positions.

Chapter 3 provides an in-depth investigation of the relationship between sustainability performance and loan spreads. We show that achieving superior sustainability performance is associated with lower, more favorable loan spreads, however we find that this only holds true when the corresponding lending bank produces good sustainability performance as well. Compared to previous research in this field, in chapter 3 we gain a deeper understanding of the causality *why* more sustainable companies receive better loan spreads by considering the sustainability behavior of the contracting counter-party. The findings provide a wide range of information relevant for practical implications. More generally, it provides insights into the

loan pricing behavior of financial institutions and helps to uncover the role of financial institutions in promoting sustainability throughout the economy. The first finding is that sustainability performance translates into better loan spreads on average. Therefore companies that are aware of this relationship should be able to improve their funding terms by strategically managing their sustainability performance. Furthermore, we show that the relationship is driven by a downside penalty for less sustainable firms, rather than an upside cost reduction for more sustainable firms. This indicates that sustainability performance should be more considered a requirement rather than a competitive edge and laggards that do not realize this yet are penalized. Furthermore, the results provide insightful information for financial institutions who may not even be aware of the differences in loan pricing between institutions. This research encourages banks and future research to investigate the creditworthiness aspect of sustainability more deeply. Our results reveal that more sustainable banks may require a risk premium, which less sustainable banks do not require. Hence, the credit pricing of less sustainable banks is more in line with that of the market. We consider though, that the market is an imperfect proxy for actual credit risk as it itself is subject to evaluation errors. Our findings highlight to policy makers the importance of encouraging sustainability performance in the financial services sectors. As key intermediaries of the economy, financial institutions play an important role in incentivizing capital market participants to transit from a myopic perspective to a long-term, sustainable business model. This is particularly important in the wake of the financial crisis, in which the trust in the global banking system has taken a great hit. Improving trust, transparency, and accountability are the path to a solid financial system.

Chapter 4 shifts the perspective from sustainability performance to sustainability disclosure. Unlike accounting disclosures, there is no set of required accounting standards that specify relevant sustainability disclosures yet. In this study, we examine whether firms that voluntarily disclose sustainability information, later identified as material by the Sustainability Accounting Standards Boards (SASB), exhibit lower stock price synchronicity. This indicates the level of relevant firm-specific information that the sustainability disclosures capture, as suggested by the standards. We show that material sustainability disclosure reduces stock price synchronicity and provide evidence which factors and conditions mediate this relationship. Our findings are relevant for policy makers, investors, and companies alike, as they signal the significance of disclosing sustainability information and evaluate the relevance of the standards. The chapter suggests that market forces, here the NGO SASB together with companies, investors, and experts in the area, can develop accounting standards that reflect investor relevant firm-specific information, complementing the regulatory process through which financial accounting standards have been developed. We show that firms with greater exposure to sustainability risks and

opportunities exhibit a strong reduction in stock price synchronicity, similarly firms that integrate financial and sustainability issues in their business have a stronger effect. For stakeholders of these types of firms, our results provide evidence that material sustainability disclosures are particularly important. Considering capital market participants, we find that both higher institutional and SRI fund ownerships magnify the synchronicity-reducing effects. An implication for firms that exhibit these investor bases is that they should consider disclosing to provide valuable firm-specific information to their investors. Furthermore, we consider the role of analysts and find that portfolio complexity moderates the relationship between sustainability information and synchronicity, revealing the information effect of sell-side analysts. Financial institutions and investors should be aware of the reduction in information-processing capabilities of sustainability information when analysts are faced with greater portfolio complexity. Finally, the chapter provides evidence on intra-industry information transfers of regulated financial information. We document higher industry-level synchronicity for firms that have low levels of sustainability information disclosure but are members of industries with relatively high levels of sustainability information disclosure. In other words, firms with few disclosures but in industries with a lot of disclosure co-move more than their industry counterparts, indicating that increasing sustainability disclosure may be even more beneficial to such firms to reduce co-movements with the respective industry.

Altogether, the studies in this dissertation provide answers to a range of pressing questions on sustainability and capital markets. The findings are relevant and can be applied to a variety of different stakeholders. Given the novelty of the research stream, there is immense value in understanding and incorporating the practical implications of this study into corporate behavior.