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## INTRODUCTION

Sustainable finance is a broad concept that refers to the alignment of the financial system with sustainability. It represents an effort to “meet the needs of the present without compromising the ability of future generations to meet their own needs.”<sup>1</sup>

It relates most to environmental issues, but it also encompasses many of the world’s current challenges.

**Ecology** – identification of ecological constraints human activity must respect

**Equity** – consideration for the needs of all (particularly the poorest)

**Intergenerational Justice** – responsibility to future generations<sup>2</sup>

In practice, there is a shift to a more holistic approach in which sustainability issues are part of the metrics. Specifically, the systematic integration of environmental, social, and governance (ESG) considerations into financial decision-making processes is labeled *sustainable finance*.<sup>3</sup>

Under the umbrella of “Sustainable Finance” is sustainable investing. According to the CFA Institute,<sup>4</sup> there are three critical elements of sustainable investing:

1. Sustainable investing is **additive to asset management theory** and does not mean a rejection of foundational concepts.
2. Sustainable investing **develops deeper insights** about how value will be created going forward using ESG considerations.
3. Sustainable investing considers **diverse stakeholders**, consistent with corporate trends.

### Weather vs. Climate<sup>5</sup>

**Weather** - represents atmospheric conditions that occur locally over short periods of time—from minutes to hours or days (e.g. rain, snow, wind, thunderstorms, etc.).

**Climate** - refers to the long-term regional or global temperature averages, humidity, and rainfall patterns over seasons, years, or decades.

**Climate change** - refers to long-term shifts in temperatures, humidity, and rainfall patterns. These shifts may be *natural*, such as through variations in the solar cycle, volcanic activity, ocean patterns, etc. But since the 1800s, *human activities* have been the main driver of climate change, primarily due to burning fossil fuels like coal, oil, and gas.<sup>6</sup>

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<sup>1</sup> Our Common Future (1987) The World Commission on Environment and Development, p. 43.

<sup>2</sup> Source: Sustainable Investing (2008) p. 3; en.wikipedia.org/wiki/Brundtland\_Commission; en.wikipedia.org/wiki/Our\_Common\_Future; en.wikipedia.org/wiki/Gro\_Harlem\_Brundtland; Retrieved May 19, 2022.

<sup>3</sup> Source: European Commission “Overview of Sustainable Finance” Available at: [https://ec.europa.eu/info/business-economy-euro/banking-and-finance/sustainable-finance/overview-sustainable-finance\\_en](https://ec.europa.eu/info/business-economy-euro/banking-and-finance/sustainable-finance/overview-sustainable-finance_en); Retrieved June 14, 2022.

<sup>4</sup> Source: <https://www.cfainstitute.org/en/research/esg-investing/sustainable-investing>, Retrieved July 17, 2022.

<sup>5</sup> Source: <https://climate.nasa.gov/global-warming-vs-climate-change/>, Retrieved July 25, 2022.

<sup>6</sup> Source: <https://www.un.org/en/climatechange/what-is-climate-change>, & UN Intergovernmental Panel on Climate Change, August 9, 2021.

*Note: Global warming* is considered one type of climate change. Heavy precipitation is another type of climate change.

*What are the current trends in the international economic and financial environment?*

- 1) A growing awareness of humankind's impact on the biosphere
- 2) An increasingly complex regulatory environment
- 3) Expanded adoption and innovation: the development of financial products to respond to environmental challenges

*What are the implications of these trends for businesses?*

- **Reporting requirements** – today it's difficult to find companies that don't report on sustainability. Pressure from investors has contributed to most of the last holdouts to increase transparency regarding their environmental impact.<sup>7</sup>
- **Risks** – many of the relevant risks are financially material to firms either as direct physical risks, which arise from climate and weather (e.g. damage from weather events, gradual changes in climate) or as indirect risks (e.g. supply-chain risks, policy risks, reputational risks, legal risks, etc.).
- **Opportunities** – consumer preferences, mitigation and adaptation efforts, and new markets (e.g. carbon markets, clean technology, sustainable fixed income, green real estate development, microfinance, etc.)

*Why is Sustainable Finance a separate course?*

In addition to the increasingly complex regulatory environment, as well as unique opportunities and risks, businesses and financial institutions rely on both natural resources and functioning ecosystems. Finally, specific investing styles and eco business models fall under the umbrella of sustainable finance.

- **Natural Resources and Business** – interactions between businesses and investment activities with natural resources is both direct (business disruptions, water use and availability, noise pollution, etc.) and indirect (supply-chain scarcities and hazardous emissions).
- **Specific Investment Styles** - ethical investing, responsible investing, ESG investing, social investing, green investing, etc.
- **Eco Business Models** – several sustainable business models exist and are becoming more widespread including: the blue economy,<sup>8</sup> traceability and sustainability certifications, and (my favorite) the circular economy.<sup>9</sup>

This course aims to help students communicate their sustainability ideas through a financial lens and to support their search for authentic, financially viable, sustainable solutions to some of our biggest environmental challenges. *Welcome to Sustainable Finance!*

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<sup>7</sup> For example, in 2019 a group of 88 investors representing \$10 trillion in assets targeted companies including: Exxon Mobil, Shell, BP, Chevron, Amazon, Volvo, Alibaba, Qantas Airways, and Genting Plantations for not reporting their climate change, water security, and deforestation data. See: <https://www.sustainability-reports.com/group-of-88-investors-target-over-700-companies-for-not-reporting-environmental-information/>.

<sup>8</sup> There is some debate as to the definition, see [https://www.un.org/regularprocess/sites/www.un.org.regularprocess/files/rok\\_part\\_2.pdf](https://www.un.org/regularprocess/sites/www.un.org.regularprocess/files/rok_part_2.pdf), Retrieved August 31, 2022. The European Commission defines the blue economy as “All economic activities related to oceans, seas and coasts.”

<sup>9</sup> The circular economy is an economic model developed in the 1950s that is becoming increasingly important, which aims to prevent waste by making products and materials more efficient and reusing them.