

The Macrotheme Review

A multidisciplinary journal of global macro trends

Shareholder Activism of Responsible Investors

Marina Milevskaya

University Of Paris 1 Pantheon-Sorbonne (Paris, France) and the National Research University "Higher School of Economics" (Moscow, Russia)

marinamilevska@yahoo.fr

Abstract

At the moment ethical principles as economic are beginning to widespread and determine the nature of the economic activity of enterprises and investment companies. The main task of ethical economy is not extending production to increase profits; it is its modernization, for example, an introduction of cleaning technologies. The presence of responsible investors between shareholders raises the question of their role in the development of an environmental policy. It represents main results of theoretical modeling and the motivation of green agents, both investors and companies. Then, on the basis of empirical analysis of the data will be made recommendations for the implementation of ethical economy's principles in the Russian conditions. We discuss whether their activism has the power to change the standards of responsible business policy. In other words, to what extent these responsible investors able to influence, for example, the choice of size of an environmental pollution. We also consider the factor of corporate reputation that influences the choice of investments and realize empirical analysis of responsible investment funds in France.

Keywords: *Green investors; ecological responsibility; socially responsible investing (SRI); environmental economics; financial markets*

1. Introduction

At the moment ethical principles as economic are beginning to widespread and determine the nature of the economic activity of enterprises and investment companies. The main task of ethical economy is not extending production to increase profits; it is its modernization, for example, an introduction of cleaning technologies. The presence of responsible investors between shareholders raises the question of their role in the development of an environmental policy. It represents main results of theoretical modeling and the motivation of green agents, both investors and companies. Then, on the basis of empirical analysis of the data will be made recommendations for the implementation of ethical economy's principles in the Russian conditions. We discuss whether their activism has the power to change the standards of responsible business policy. In other words, to what extent these responsible investors able to influence, for example, the choice of size of an environmental pollution. We also consider the factor of corporate reputation that influences the choice of investments and realise empirical analysis of Responsible investment funds in France. It permits to offer recommendations for the successful implementation of the principles of ethical economy in the other international markets.

2. Literature review

The paper of Meir Statman (2000) [1] describes two main effects of the actions of responsible investors:

1. Investment actions effect.
2. Effect of policy.

Andrea Beltratti (2003) [2] constructs a macroeconomic model to find the general equilibrium with SRI. The model has two heterogeneous agents, two periods and two types of securities (irresponsible stocks and "safe" bonds). It examines the impact of SRI on the price of the securities. Important factors in the model are wealth of responsible investor and diversification opportunities. One way, the relative size of the wealth of economic agents is crucial. And another way if the company has the unique traits to become the subject of diversification, it has no strong incentive to be more responsible. The agent made the choice of consumption and investment. The author analyzes the impact of the heterogeneity of agents and externalities of production (as an indicator of corporate social responsibility). It is assumed that the production function depends directly on the loans and specific exogenous shock for each company (negative and positive). The authors consider the externality associated with the specificity of socially responsible investments, in this particular case they interpret it as the negative effect of demand of loans from the company A ("polluting industry") on the utility of agent *i* ("responsible investor"). The model is simple and it can not show any significant consequences. It concludes that SRI does not have strong impact when the number of responsible investors is small and there is a lot of possibilities for diversification.

In the following papers (2010-2011) [3], [4] Lammertjan Dam, Ben J. Heijdra provide the conception of "warm-glow effect" developed by James Andreoni in 1990 to explain impure altruism. Instead of being only motivated by an interest in the growth of welfare of recipients of investments, the "warm-glow investors" have also the utility of the act of giving, that is to say, they have a selfish motivation. This motivation can arise, for example, from the desire to have a reputation of socially responsible people or philanthropists. These papers analyze the impact of SRI on quality of environment and abatement economy. The authors examine whether environmental policy is effective when consumers themselves have an incentive lied to the "warm-glow motive" to internalize the environmental externalities in their functions. It is found that their responsible behavior partly ensure the positive effects on environmental quality of the abatement policy. The "warm-glow" motivation imposes an implicit tax on the value of the polluting company. It assumes that investors can choose only the "pure" bonds or stocks of irresponsible corporations. The effect of warm-glow requires a growth of premiums to induce them to purchase these shares. The paper assumes also that there is no risk, so the bonds and stocks are perfect substitutes and moreover it analyzes the consequences of two environmental chocks: (1) The continued growth of non-expected level of public abatement financed by taxes and (2) the temporal increase of "warm-glow" parameter.

The impact of the actions of responsible investors on business decisions and social policy is also examined by Amir Barnea, Robert Heinkel and Alan Kraus in the paper of 2005 [5]. There are three categories of companies: polluting, clean and reformed, and two types of investors: neutral and green. The authors find the Nash equilibrium for three levels of capital costs. When the costs of reform are small responsible investors can significantly change the economic situation, investments in irresponsible companies fall which reduces the total investment. If these

costs are large, responsible investors lose power. If costs are middle, the economy receives the maximum of investment if there are only responsible or irresponsible investors.

Now we can consider the paper lied with an activism of general shareholders. Ernst Maug [6] examines the role of liquidity in financial market in surveillance of company policy. He assumes that the greater liquidity should discriminate against the desire of large shareholders to participate in the management of the company. However, the results of model show that there is the positive impact of liquidity on corporate control. In this paper he constructs theoretical economics and the process of decision-making to discuss the effect of the presence of "blockholders". The concept of "monitoring" is used synonymously with "shareholder activism". There is a problem of free-riding because small shareholders benefit from the efforts of large investors and do not pay for it. We analyze the equilibrium size of the major shareholder, he brings two effects: "lock-in-effect" (the ability to control has value) and "liquidity effect" (in the stock market after buying large shares there are few stocks which reduces liquidity). The other unobvious result: the liquid market allows to solve the problem of free-riding, because in the less liquid market the potential shareholders do not want to buy a lot of stocks to avoid problems of inflexibility.

Finally we consider the literature related to the analysis of the role of reputation. Previous research generally assumes that a good reputation is a resource of competitive advantage. In her paper Sabrina Helm (2007) [7] defines reputation as "the business valuation carried out by its shareholders", according to their affect and knowledge. She argues that reputation is an intangible asset of the company. Helm also adds that reputation is a socially shared image and a consensus on what is his behavior in a given situation. It is based on collectively held expectations about the ability of a company and its willingness to satisfy the interests of different agents, for example, those of consumers, investors and suppliers.

3. Empirical analysis

In ethical economy green investors and enterprises apply policies to improve the environment or implement responsible social policy. In making the decision to invest green investors typically consider not only economic but also ethical factors of the companies. Ethical factors can be divided into social and environmental. The first subgroup includes, for example, the terms of the material and immaterial compensation, equal opportunities for men and women, cultural and sports events for employees, charitable activities of the company. The second subgroup includes information on industrial waste, modernization of production technology, the company's position in relation to the national policy of environmental protection.

We analyze socially responsible investment funds and shareholders of the companies operating in France. There are thirty official green funds. However, even the French-born funds prefer to invest in foreign companies. The average portfolio consists of 50 securities, of which an average only 7 issued by French companies, less than 15%. This situation, in view of the fact that analyzes the development of the economy, makes us think that the ethical economy as a whole is at an early stage of development. An analysis of the portfolios selected 70 French companies which are attractive.

One of the main tasks was research of the activity and principles of the main shareholders of companies. Among twelve green enterprises, that are enterprises engaged in the processing of industrial waste and the production of solar and wind energy, only one has as a major shareholder an official green fund (Suez Environment). It should be noted that among the main shareholders

of the eight green companies there are not any green agent, and the State participates in the activities of only four companies. As a rule, most of the securities remain on the hands of business owners, forcing companies to invest in modernization of production. Among the 58 largest shareholders of reforming enterprises are only four companies are held by green funds. The State is involved in the board of shareholders of 21 companies that can make a general conclusion that the ethical economy as a whole was created because of government intervention.

4. Implications for investors and conclusion

In other countries, developed and developing, for example, in Russia the State also owns shares in key companies, and it is logical to assume that the state is able to give impetus to the development of ethical economy. However, one can not deny the importance of the responsible investment funds. Judging by the amount of foreign securities in the portfolio of French funds, t

It may be noted two trends. The positive trend is that the government can influence the formation of ethical economy through participation in the activities of polluting companies, which is also applicable in the Russian reality, where the government owns shares of all key companies in the national economy. The negative trend is the fact that even in a developed country as France the choice of objects for green investment is not easy. In Russia, the establishment and development of ethical economy will emerge by French scenario: public-private enterprises will advanced in promoting of an ethical corporate policy, and the existing or emerging green funds start its activity by large international diversification to form a well-diversified portfolios. The study shows the potential for an ethical economy development and the possible fast and big growth of the number of enterprises using a responsible corporate policy.

References

- [1] Statman, M. (2000): *Socially responsible mutual funds*. Financial Analysts Journal, 2000, 30–39.
- [2] Beltratti, A. (2003): *Socially responsible investment in general equilibrium*. Nota di Lavoro, 2003, 93.
- [3] Dam, L. - Heijdra B. J. (2011): *The environmental and macroeconomic effects of socially responsible investment*. Journal of Economic Dynamics & Control, 2011, 35 : 1424-1434.
- [4] Dam, L. - Heijdra B. J. (2010): *The environmental and macroeconomic effects of socially responsible investment: Mathematical Appendix*. 2010, www.heijdra.org.
- [5] Barnea, A. - Heinkel, R. - Krause, A. (2005): *Green investors and corporate investment*. Structural Change and Economic Dynamic, 2005, 16 (3), 332–346.
- [6] Maug, E. (1998): *Large shareholders as monitors: is there a trade-off between liquidity and control?* Journal of Finance, 1998, 53(1), 65-98.
- [7] Helm, S. (2007): *The role of Corporate Reputation in Detemining Investor Satisfaction and Loyalty*. Corporate Reputation Review, 2007 Vol.10, No.1, pp. 22-37.