Geeta Aiyer's Acceptance Remarks:
2015 Joan Bavaria Award

Checks and Balances: The Role of Investors in Guiding Financial Markets to Sustainability

Transcript of remarks by Geeta Aiyer, President and Founder, Boston Common Asset Management on the occasion of receiving the Joan Bavaria Award

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Thank you for this exceptional honor. As someone who knew and admired Joan Bavaria, I feel honored to accept this special award founded in her name. Joan was that rare human being who combined analysis and intellect with a startling capacity for vision and creativity. She began her career as an artist, and although she eventually became a leader in the investment world, she never lost the ability to see the essence of a problem or to imagine a bold, new future.

We all know that we are in the midst of rapid change, change that can only be navigated if we understand our destination, and if we are willing to make course corrections along the way. We are charged with effecting radical change, as stewards of a transition to a more sustainable model, in the face of extreme economic and ecological debt. We must embed these changes in our systems and structures, and in the very cultures of our organizations. Time is short. We will need the vision, the capacity for reimagining, the daring and tenacity, and the hope and faith that Joan embodied.

It is in this spirit that I would like to speak to what our movement has become and where, through our continued hard work, it might go.

It is sometimes hard to remember that change has always been rapid. Many of the features of the capital markets that we take for granted today are relatively new inventions. Managerial and cost accounting arose in the 20th century. Modern Portfolio Theory, the Capital Asset Pricing Model, and FASB came into being in the 50's, 60's and 70's. Mutual funds took off in the 1980s, followed by hedge funds, and all manners of complex mechanisms–innovations that

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reached a dizzying pace, “financializing” every kind of transaction. Their scale and collective error nearly brought the entire system down.

We need financial creativity and innovation redirected.

The capital markets lost track of some fundamental principles of investment and ownership that, if properly understood and practiced, can guide our whole economy to sanity and sustainability.

These principles, fortunately, lie at the heart of responsible investment. They include:

1. the core idea that owners of shares are owners of the corporation–and that they have duties and opportunities that flow from that special status.
2. the notion that equities are fundamentally a long-term asset class, through which the interests of shareholders should align, over time, not only with those of the corporation, but also with society.
3. the concept that not everything can be immediately or perfectly quantified–and that critical pieces of information may be overlooked or rejected as non-material if we wait for perfection;
4. the understanding that institutions with substantial equity holdings share a permanent, structural interest in the long-term health of our ecosystems and economy.

Over the last decades, we have seen a convergence of mathematical skill and computing power into investing. While we harness this tremendous power in our work, we cannot become bound and habitual in the variables we consider and scenarios we model.

The task of the investor always involves judgment. Truly great investors are middle-aged, like me! They have bifocal lenses, so they can push back their chair from the models on the screen—to think about what they are seeing, to let go of the past and ponder the future, to imagine how a company, an industry, or an entire economic or ecological system would function if assumptions were to change or trends accelerate.

One of the purposes of a long-term horizon and deeper investigation is to correct and withstand tracking error. It is the role of the analyst—equipped with the tools provided by financial analysis and ESG–to ferret out information, to identify hitherto unappreciated relationships, and to create a new formula, a new “secret sauce” that correlates metrics, factors, and information.

The ESG lens also allows investors to see emerging realities, not yet deemed material. We can then assess the probabilities, the scenarios, the distributions, the discount rates, and the risks. From all of this careful thinking by many parties, we can move away from the reflexive, and frequently counterproductive, emphasis on simple metrics that reinforce destructive, short-term, quarter-to-quarter thinking. To this end, any here have been working towards integrated reporting to combine financial and sustainability information in a usable way, tracking all outcomes of corporate activity in one place.

Most of all, good shareowners need to maintain solid reference points—we might even call them values—about economy, a healthy planet, and genuine prosperity. They must be able to see a company's business plan—or an industry's evolution—in the wider context of economic, environmental, and financial stability.

I have tried to build this fundamental philosophy going back to the founding of two firms: Walden and Boston Common. Indeed, in naming both of these firms, I hoped to make a subtle statement about the values that I think are essential to a healthy economy. I chose the name "Walden," to refer to the independent thinking and naturalist passion of Henry David Thoreau, a man who believed in the "majority of one," who was willing to stand up to prevailing opinion even to the point of civil disobedience. He also stood for frugality, low resource intensity, doing more with less, and resourcefulness–all qualities we need to reaffirm today. There was even a small connection to early globalization and to me! I have always found it amazing that ice cut from Walden and other ponds in Massachusetts was packed in sawdust and shipped all the way to Madras, India, so that the British could enjoy cold drinks as a perk of colonial rule!

Similarly, in choosing Boston Common, I wanted to honor an old and vital concept to which we must also return—the concept of the commons. Boston Common was established in 1634 as a protected space and a resource that belonged to no one but was important to all. Nearly 400 years ago, in my adopted hometown of Boston, citizens were willing to pay for something that had public benefit.

We all should be encouraged and proud of the transformation we have seen in the last two decades. It is remarkable that in the U.S. $6.5 trillion dollars—almost 18% of all invested assets—are now invested in responsible portfolios. But in some ways, we are still at the beginning. Using ESG criteria is not just a product or a clever way of sorting companies into better and worse performers; it is a lens through which we can understand the creation of value and the direction of the economy at a more fundamental level.

We should all be concerned that ESG analysis has only a new but very small place in the curriculum and exams to become a Certified Financial Analyst. That needs to change.

Because of the speed of innovation and the general paralysis of political institutions, we need new mechanisms to guide the powerful technological and market forces that are reshaping our planet. Capital markets have immense power, but left to themselves without thought, without intentionality, without purpose, they can revert to destructive, short-term thinking.

Corporate managers can act as if they are playing a one-time game with the intent to maximize and take all. It is up to shareowners to point out that we are engaged in a long-term “repeat game” where sustainable reasonableness is rewarded. Thus we must counteract the huge pressures that corporations face to externalize their costs and to maximize their returns over the short-term.

We know that problems intensify when ownership and control drift apart. Our movement is about continuously bringing them back together. And in doing so, we actually make markets more efficient.

In the short-term, markets tend to be confused, unable to sort out all the different inputs and implications, to discern the signal from the noise. In my view, true market efficiency depends on active investor participation: active investing with analysis and judgment and active engagement with clarity of purpose. This does not happen without effort.

In other words, active investors and asset owners, with a deep and long-term understanding of prosperity, can use ESG analysis and direct engagement to provide the critical checks and balances that financial markets require to function as efficient and socially beneficial distributors of capital.

Joan Bavaria would be proud and astonished of how far we have all come over the last 25 years. But she would also be the first to point out that we still have a long way to go. The challenges ahead of us—from global inequality to resource depletion to climate change and beyond—will require every ounce of our combined commitment and talent. 2015 will be an important year as we move towards the Paris conference on climate change in December; all of us involved in sustainability must redouble our efforts to show that the transition to a low-carbon economy can be a quick and smooth one.

I have always been inspired by the words of Martin Luther King who said, “In the end, we will remember not the words of our enemies, but the silence of our friends.” What gives me hope today is that when it comes to the most pressing problems of humanity, we as a community have never been silent. Today, more than ever, the world needs to hear from us, and looking around the room, I have confidence that it will.

Thank you very much.