

Funds with Benefits: Exploration of Underlying Drivers of Article 9 Bond Funds and the Impact of SLBs

A qualitative study based on a case study of Lannebo's Article 8 Sustainable Corporate Bond Fund and interviews with Nordic Article 9 Fund Managers

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Master's Thesis

Department of Finance Stockholm School of Economics

May 2024



Abstract

In March 2021, the European Commission introduced the Sustainable Finance Disclosure Regulation (SFDR), mandating fund managers within the EU to categorise their products into Article 9 (dark green), 8 (light green), and 6 (other). This paper aims to understand the motivations behind fund managers' decisions to launch Article 9 corporate bond funds and explore whether Sustainability-Linked Bonds (SLBs) have facilitated the adoption of these funds. Furthermore, a case study of Lannebo Fonder, managing an Article 8 corporate bond fund, complements the insights gained from managers managing Article 9 funds. A qualitative analysis has been conducted with 15 interviewees, including fixed-income fund managers and other stakeholders, to capture diverse perspectives. First, we find that fund managers initiating Article 9 corporate bond funds are motivated by three primary factors: (1) Growing investor demand, particularly among institutional investors, who prioritise factors beyond profit maximisation, (2) Fund differentiation opportunities which arise from the SFDR labelling system, (3) SFDR enhances market transparency, pressuring fund managers to issue Article 9 funds for reputational reasons. We further find an additional partial contributory factor: Article 9 bond funds have a swifter and increased impact while being at a lower risk than Article 9 equity funds. Second, we find that SLBs contribute to the ability to launch *high-yield* Article 9 corporate bond funds, given that companies with higher credit risk profiles tend to issue them. Nevertheless, SLBs present several drawbacks, such as challenges in tracking their proceeds attributable to insufficient transparency, elevated risk of greenwashing, and heightened analysis efforts compared to *use-of-proceeds*. Third, the case study of Lannebo shows that Article 8 corporate bond funds can integrate sustainability and prioritise returns, leveraging less stringent sustainability disclosures than Article 9 funds. However, fund managers aiming to start sustainable corporate bond funds today will likely increase investor attractiveness with the Article 9 label.

Key Words: Case study, SFDR, Article 9 funds, Bond funds, Sustainability-linked bonds

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Acknowledgements: First and foremost, we thank our thesis supervisor, Per Strömberg, for his unwavering support and constructive feedback. Moreover, we would like to express our gratitude to all fund managers and other interviewees who contributed to our thesis with their knowledge, insights, time, and feedback.

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Abbreviations

AUM = Assets Under Management

CSRD = Corporate Sustainability Reporting Directive

ESA = European Supervisory Authorities

ESG = Environmental, Social, Governance

EU = European Union

FA = Financial Adviser

FMP = Financial Market Participant

KPI = Key Performance Indicator

SFDR = Sustainable Finance Disclosures Regulation

SPO = Second Part Opinion

SLB = Sustainability-Linked Bond

SPT = Sustainability Performance Target

SRI = Socially Responsible Investment

PAI = Principal Adverse Impacts

RTS = Regulatory Technical Standards

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1. Introduction

In response to pressing societal challenges such as climate change, sustainable finance has emerged as a tool for the financial sector to promote sustainable projects (Bakken, 2021). Sustainable finance has reshaped debt markets over the past decade and driven several financial innovations, resulting in a substantial expansion in the sustainable debt market (Cochelin et al., 2024). In particular, the sustainable bond market has experienced 188% growth from 2019 to 2023 (ibid). With the escalating awareness regarding the need to combat societal challenges and the growing sustainable bond market, financial market participants' (FMPs) attention has been captured, compelling a shift towards sustainable bond funds (Kirstein, 2021). Article 9 funds represent the latest approach to labelling sustainable funds within the sustainable bond fund market. With cumulative flows going into each fixed-income Article 9 fund from January 2019 to July 2023 being 2.1x higher than its non-sustainable counterpart (Tylenda et al., 2023). The Article 9 label originates from the Sustainable Finance Disclosure Regulation (SFDR) introduced in 2021, stipulating disclosure requirements for all FMPs. The central aspect of the SFDR is the classification of funds based on their level of commitment to sustainability, designated as Article 6, 8, or 9 (Bengo et al., 2022). The main distinction lies in the focus of the funds: Article 8 (light green) funds promote environmental or social characteristics, while Article 9 (dark green) funds have sustainable investment as their primary objective. Article 6 (other) funds neither prioritise nor promote environmental or social characteristics. Ferriani (2023) and Scherer & Hasaj (2023) show evidence that the Article 9 label significantly increases net capital inflow. However, focusing on Article 9 bond funds, little is known about this fund type, noting the limited available literature on sustainable bond funds in general. Moreover, the underlying motives behind fund managers' decision to issue an Article 9 bond fund remain ambiguous, and further research is warranted.

Furthermore, Article 9 bond funds allocate investments across various sustainable debt instruments, with sustainability-linked bonds (SLBs) being the youngest bond type (Vulturius et al., 2024). SLBs are bonds distinguished by their financial and structural features, which may fluctuate based on the issuer's attainment of predetermined sustainability objectives (ICMA, 2023a). Existing literature has shown that SLBs are gaining popularity as this instrument offers greater flexibility in utilising the proceeds than green or social bonds (Liberadzki et al., 2021). Despite greater flexibility, SLBs comprised 7% of the ESG bond market 2023, while green bonds accounted for almost 60% of all ESG bonds issued (Cochelin et al., 2024). Some investors are sceptical about whether SLBs are the "*right shade of green*" for sustainable bond funds, where the risk of greenwashing is the main worry (Albuquerque, 2023). Despite the growing prevalence of SLBs, there remains a scarcity of knowledge surrounding this emerging financial instrument, warranting research in several fields. For example, it is unclear how SLB characteristics fit within Article 9 bond funds and if they have impacted the Article 9 market.

This thesis examines the determinants that drive fund managers' decision-making process in issuing an Article 9 corporate bond fund over an Article 8 counterparty. We aim to clarify the rationale behind such choices and evaluate the associated advantages and disadvantages. We have chosen to focus on Nordic bond fund managers to limit the scope and facilitate access to interviewees. Moreover, we investigate SLBs' implications in this market in an attempt to conclude if SLBs can be a reason or facilitator for issuing Article 9 corporate bond funds. Thirdly, we conduct a case study of Lannebo Fonder and examine their decision to launch a sustainable corporate bond fund and make it an Article 8 fund instead of Article 9. This seeks to examine if their decision relates to previous literature and how SLBs have influenced their operations to provide a practical instance. To gain this perception, this thesis aims to answer the three research questions presented below:

1. *What key drivers lead Nordic bond fund managers to issue Article 9 corporate bond funds?*
2. *What implications do SLBs have for the Article 9 corporate bond fund market?*
3. *What insights can be gained from Lannebo's Sustainable Corporate Bond fund, examining the trade-offs for fund managers between Article 8 and 9 corporate bond funds?*

We present empirical findings on the three research questions concerning Article 9 corporate bonds and SLBs, using responses from 15 interviewees. First, we find support that fund managers launch Article 9 corporate bond funds driven by three primary factors: (1) Growing investor demand, particularly among institutional investors, who prioritise factors beyond profit maximisation, (2) Fund differentiation opportunities which arise from the SFDR labelling system, (3) SFDR enhances market transparency, pressuring fund managers to issue Article 9 funds for reputational reasons. A partial contributing factor is Article 9 bond funds' swifter and increased impact while being lower risk than Article 9 equity funds. Second, we find that SLBs contribute to the ability to launch *high-yield* Article 9 corporate bond funds. SLBs are commonly issued by smaller firms with low credit ratings seeking to enhance their sustainability efforts. This aspect fills a gap that *use-of-proceeds* bonds cannot address, as *use-of-proceeds* typically have investment-grade credit ratings. Interviewees, moreover, suggest that SLBs with relevant KPIs can have a greater impact than the *use-of-proceeds* format. Therefore, Article 9 funds incorporating these SLBs can achieve greater sustainability impact. Nevertheless, SLBs present several drawbacks, such as challenges in tracking their proceeds due to insufficient transparency, elevated risk of greenwashing, and increased analytical demands compared to *use-of-proceeds*. Finally, the case study of Lannebo shows that Article 8 corporate bond funds can integrate sustainability and prioritise returns, leveraging less stringent sustainability disclosures than Article 9 funds. However, Lannebo has experienced low demand for its Article 8 bond fund since its launch. In contrast, Article 9 fund managers have shown a high demand for their funds during the same period. This suggests fund managers aiming to start sustainable corporate bond funds today will likely increase investor attractiveness with the Article 9

label. An action that fund managers are incentivised to take as their goal is to boost total fund assets (Chevalier & Ellison, 1997).

This thesis aims to contribute to existing research in several ways. First, focusing on addressing Article 9 funds, the literature indicates that the Article 9 label can enhance net fund flow (e.g., Ferriani, 2023; Scherer & Hasaj, 2023). However, we do not find prior research examining the market dynamics influenced by SFDR and investigating the factors influencing the decisions of some fund managers to launch Article 8 funds while others opt for Article 9 funds. Hence, a gap within this field exists on what drives fund managers in this decision-making process. Second, this study aims to fill a gap in the field of sustainable bond funds, noting the limited research field of bond funds in general compared to equity funds. With the substantial growth witnessed in the sustainable bond market, much activity is occurring within this segment. Third, given that SLBs are the latest inclusion in the sustainable debt market with limited research, it presents an opportunity to explore their implications on Article 9 bond funds. Existing literature highlights concerns about the flexible structure of SLBs, such as lack of transparency over the proceeds (e.g., Liberatore, 2021; Berrada et al., 2022; Kölbel and Lambillon, 2022; Vulturius et al., 2024). Therefore, this study contributes to analysing SLBs in this context. To our knowledge, we are the first study to empirically investigate the implications of SLBs on Article 9 bond funds.

The rest of the paper proceeds as follows. Section 2 delves into the SFDR fund landscape to offer contextual information and background. In Section 3, we conduct a literature review addressing the primary drivers influencing fund managers' portfolio management. Subsequently, it narrows the focus to examine the existing literature on the factors influencing fund flows into sustainable mutual funds. It additionally raises the investor and issuer perspective of sustainable bonds. Section 4 outlines the methodology used for the case study and the qualitative research. In Section 5, we conduct a qualitative comparison between Nordic fund managers and their drivers for issuing an Article 9 corporate bond fund. Section 6 presents the results of our case study. Finally, we discuss our results in Section 7 and present our concluding remarks and ideas for further research in Section 8.

2. SFDR Fund Landscape

This section presents an overview of the SFDR fund landscape and the global sustainable debt market to explore the evolution of the sustainable bond fund market after SFDR was implemented. This further lays a foundation for understanding which investments are included in sustainable bond funds for later results in Section 5.0. The section begins by providing an overview of the evolution of the EU's sustainability regulations to understand the implications of these regulatory changes for funds with a sustainability focus.

2.1 EU Sustainability Regulations

In 2018, the European Commission's action plan on Financing Sustainable Growth was adopted with ten key actions, aiming to increase capital flows to more sustainable investments. This section will focus on three central parts of this action plan: the Sustainable Finance Disclosure Regulation, the EU Taxonomy for Sustainable Activities, and the Corporate Sustainability Reporting Directive.

2.1.1 *The Sustainable Finance Disclosure Regulation (SFDR)*

Background

In 2019, the European Commission announced the SFDR when they adopted regulations 2019/2088 (the SFDR) and 2019/2089 (the Benchmark Regulation). However, it was not until March 2021 that they finalised and introduced the first level ('Level 1') of SFDR (ICMA, 2021). The purpose of the regulation is twofold: to increase sustainable investment by providing transparency to investors and to decrease greenwashing (Swedish Financial Supervisory Authority, 2022). SFDR addresses crucial aspects such as integrating sustainability risks, considering adverse sustainability impacts, promoting environmental or social characteristics, and fostering sustainable investments (ibid). SFDR is the first mandatory ESG regulation in the EU and mandates specific guidelines for market participants regarding the disclosure of sustainability-related information.

To complement the initial 'Level 1' of SFDR, the European Commission authorised the European Supervisory Authorities (ESA) to create draft regulatory technical standards (RTS). The RTS can be seen as 'Level 2' of the SFDR implementation and disclosure requirements, which was implemented in January 2023 (ESA, 2021a). This second level outlines applicable principal adverse impacts (PAIs) and their appropriate metrics and provides reporting templates for the quarterly PAI statements (ibid). The PAI indicators are a set of compulsory (14) and voluntary (31) metrics and indicators whose goal is to transparently show how investments can pose sustainability risks (Vanhomwegen, 2021). Three examples of compulsory indicators are water pollution, greenhouse gas emissions, and weapon production (ibid). See the complete implementation timeline of SFDR in Appendix 1.

Entity Level and Product Level

The SFDR categorises financial intermediaries into two types: financial market participants (FMPs) and financial advisers (FAs) (Swedish Financial Supervisory Authority, 2022). FMPs and FAs must disclose sustainability information on entity and product levels (see Appendix 2). This thesis focuses on FMPs within the framework of SFDR, given that fund managers fall under this category. To comply on an entity level, FMPs need to publish information as named in Articles 3-5 (Bengo et al., 2022). The Articles include publishing how they work with sustainability risks in their decision process (Article 3), if they assess the adverse impacts (PAI) affecting sustainability factors and

incorporate these assessments into their due diligence policies (Article 4), as well as ensure that their remuneration policies align with the integration of sustainability risks (Article 5)(ibid).

Regarding product level disclosure, there are three levels of Articles: 6, 8, and 9. This is a self-assigned classification system, with each classification step increasing reporting obligations and sustainability classification (Bengo et al., 2022). Transparency regarding integrating sustainability risks into the investment process and considering PAIs (Article 7, product level disclosure of PAI) applies to all FMPs and financial products. Nevertheless, it differs between Articles 6, 8, and 9. Therefore, FMPs must explicitly explain why their financial products are classified as different articles using the respective templates and metrics (ESA, 2021a).

Article 9 (dark green) pertains to funds with sustainable investment as their primary objective, with the highest requirement for reasoning why their financial products are classified as sustainable. According to SFDR, sustainable investments are defined as investments in companies or other economic activities that (a) directly contribute to an environmental or social objective, (b) do not significantly harm any of these objectives, and (c) pursue good governance. Therefore, these funds aim to generate environmental or societal impact, contributing to sustainability and actively prioritising sustainability for fund managers (Swedish Financial Supervisory Authority, 2022). In contrast, Article 8 (light green) applies to financial products that promote environmental or social characteristics. These funds do not have ESG investing at their core as they promote ESG alongside financial objectives. However, the SFDR does not specify how to promote environmental or social objectives, leaving the classification decision to the discretion of FMPs. Promoting environmental or social objectives can be achieved, for example, by only employing tools such as exclusion or screening (ESA, 2021b). Today, the market divides Article 8 funds into Article 8+ funds and Article 8 (no SI) funds. Article 8+ funds are those who have ‘sustainable investments’, while Article 8 (no SI) are Article 8 funds without sustainable investments (Tylenda et al., 2023). When referring to Article 8 funds, it encompasses both those labeled as Article 8+ and those designated as Article 8 (no SI) (ibid). Article 6 (grey) funds neither prioritise nor promote environmental or social characteristics.

Article 6 funds must either publish a PAI statement or explain their choice not to (ESA, 2021a). In the supplementary disclosures for Article 8 and Article 9 funds, they must employ the PAIs, their appropriate metrics, and provide filled reporting templates for the quarterly PAI statements (ibid). In contrast to Article 8 funds, Article 9 must ensure and continue to ensure that the companies included in the fund are EU Taxonomy-aligned. The FMPs define whether a company can be considered aligned until the Taxonomy and CSRD are fully incorporated (see Sections 2.1.2 and 2.1.3).

SFDR Limitations and Interpretation

One drawback of SFDR lies in the self-assessment conducted by FMPs regarding the sustainability of their offerings, as the categorisation of funds into Articles 6, 8, or 9 is not carried out or verified by an independent third party (Noonan, 2021). Moreover, while SFDR establishes compliance requirements for the various article classifications, uncertainties remain regarding the precise definitions of products categorised under Article 8 or 9. Focusing specifically on Article 8 funds, there is a lack of clarity on what constitutes the promotion of environmental or social activities (Rust, 2022). All bonds held in an Article 9 bond fund must be sustainable, while an Article 8 bond fund may hold any type of bond as long as it does not do any significant harm and promotes environmental or social characteristics, which is up for interpretation. Consequently, Article 8 classified financial products exhibit significant variability in sustainability levels (Meager, 2021).

Additionally, before the definitive release of the RTS (in 2023), FMPs were unaware of the obligation to disclose PAI metrics and other quantitative data at the product level. This ambiguity led to divergent interpretations and inconsistencies in disclosures among these articles (Noonan, 2021). As Article 9 funds' commitment to sustainability should be the priority of the fund managers, this further requires deeper disclosure requirements for Article 9 funds to defend their sustainable investments (aligning with Article 7). Consequently, there was a specific wave of downgrading by fund managers from Article 9 to Article 8 when the second level of SFDR was implemented (January 2023) when it started to become required for fund managers to disclose more information regarding their ESG methodologies, sustainability risks, and impact in pre-contractual documents and periodic reports (Englundh, 2023). Therefore, due to Article 9 fund managers' trepidation about investing in non-sustainable companies that fail to meet the SFDR standards, they frequently opt for "safer" alternatives instead of investing in transition companies (Albuquerque, 2023).

2.1.2 EU Taxonomy for Sustainable Activities

The EU Taxonomy came in 2020. It guides FMPs in assessing the environmental sustainability of their investments and was created to give a unified definition of what "sustainable" means (European Commission, n.a). This partly mitigates the limitations of SFDR itself as the Taxonomy alignment of investments is then required for the SFDR and CSRD reporting.

The Taxonomy Regulation set up four conditions to qualify as environmentally sustainable and therefore align with the taxonomy: (1) substantial contribution to one of the six environmental objectives, (2) no significant harm on any of the other five environmental objectives, (3) compliance with minimum (social) safeguards, (4) compliance with technical screening criteria specifying point (1) and (2) (ibid). Furthermore, it established six objectives, including a list of sustainable activities, to specify how different activities can contribute to each objective. These six objectives are (1) climate change mitigation, (2) climate change adaptation, (3) sustainable use and protection of water and marine resources, (4) transition to a circular economy, (5) pollution prevention and control, and (6) protection and restoration of biodiversity and ecosystems (ibid).

2.1.3 *Corporate Sustainability Reporting Directive (CSRD)*

CSRD was presented in 2023 and is the latest implemented regulation. However, the regulation comes into force in the fiscal year of 2024, and therefore, the first reports with CSRD information will be published in 2025 (ESMA, n.a). This new regulation is replacing its predecessor, the Non-Financial Reporting Directive (NFRD), which outlines regulations for the social and environmental disclosures companies must make. CSRD mandates companies to disclose information about their social, environmental, and governance practices, enhancing transparency and accountability in corporate activities. This disclosure is relevant for FMPs as it provides them with data to assess the sustainability performance of companies where they invest, increasing transparency in the market. The CSRD complements SFDR as it supplies data for SFDR reporting. With the implementation of the new CSRD, the Taxonomy will go from covering 11,000 companies to gradually covering 50,000 organisations (European Parliament, 2022). See Appendix 3 for a summary of the relationship between SFDR, the Taxonomy and CSRD.

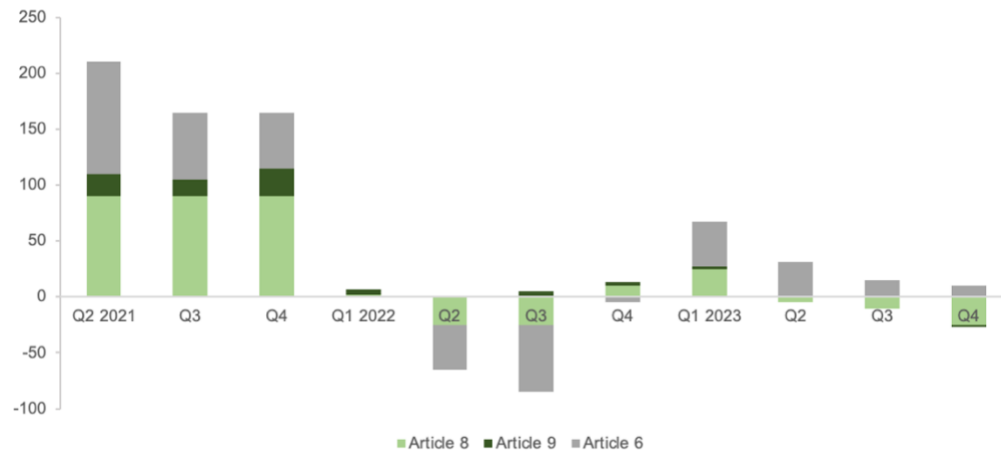
2.2 Evolution of the SFDR Fund Landscape

Since the implementation of SFDR in 2021, Article 9 and 8's cumulative fund flows for mutual funds have been greater than Article 6's (see Figure 1). For specifically fixed-income funds, one can again see that Article 8 and 9 funds surpassed non-ESG peers (Tylenda et al., 2023). In addition, cumulative flows going into each fixed-income Article 9 fund from January 2019 to July 2023 was 2.1x higher than for Article 6 funds (ibid). The organic growth rate of quarterly flows for Article 9 funds has consistently outpaced that of Article 6 and 8 funds until Q3 2023 (see Figure 2). Furthermore, Article 9 funds have been the only resilient fund type on the fixed-income side over the years, seeing a net inflow of USD 16 billion between January 2022 and July 2023, while Article 8 funds experienced net outflows of USD 16 billion (see Appendix 4). However, Article 9 funds' performance has been historically shown to be more volatile than Article 8+ funds (see Appendix 5). Moreover, Article 8+ fund performance slightly dropped below the median in 2023 (see Appendix 5).

Throughout 2023, the bulk of net savings in Sweden went into Article 8 funds, receiving a substantial SEK 109 billion influx (Swedish Investment Fund Association, 2024a). Sweden has the highest proportion of Article 8 funds across Europe, signalling its leadership role in sustainability (see Appendix 6). Looking at Sweden's fund type breakdown, Article 8 funds dominated the fund landscape, capturing 73% of the total fund market (by number of funds) by December 2023, compared to 43% in Europe overall (see Figure 3).

Figure 1

Quarterly Flows Into Article 8 and Article 9 Funds Versus Article 6 Funds (EUR Bn)

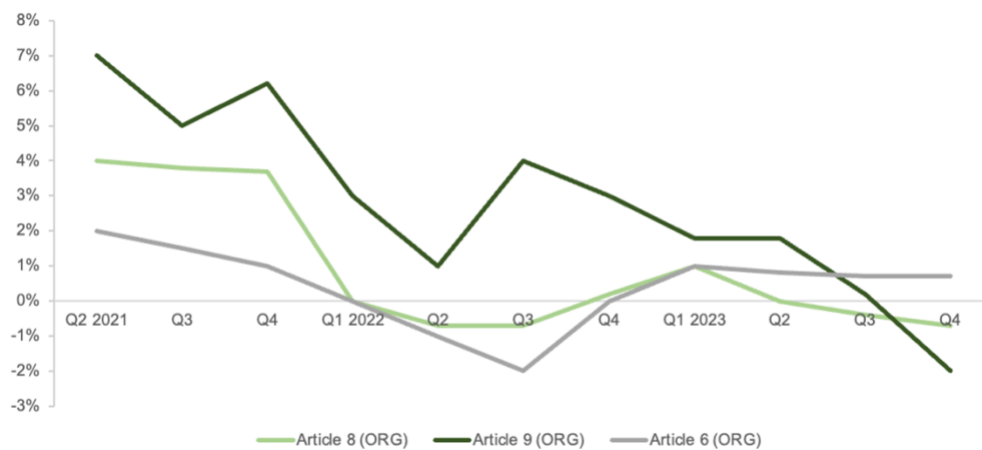


Source: Bioy et al. (2024)

Meanwhile, Article 9 funds secured a 6% share of the total market and saw a net inflow of SEK 9.4 billion (Swedish Investment Fund Association, 2024a). Focusing specifically on long term bond funds in Sweden, Article 9 funds in this category increased from 5% to 8% between 2022 and 2023, signalling rising enthusiasm for sustainable investments (Swedish Investment Fund Association, 2024b).

Figure 2

Quarterly Flow Growth Rates Article 6, 8 and 9 funds Europe (%)



Source: Bioy et al. (2024)

Figure 3
SFDR Fund Type Breakdown (by Number of Funds) in 2023 (%)



Source: Swedish Investment Fund Association (2024a); Bioy et al. (2024)

2.3 Sustainable Debt

Given the paper's emphasis on Article 9 corporate bond funds, another aspect to consider is how these funds allocate capital to different sustainable debt instruments. Subsequent sections will, therefore, further detail the sustainable debt market.

2.3.1 Background to Sustainable Debt

Sustainable debt can be summarised as when an issuer takes a loan or issues a bond to invest in specific projects or in their operations to promote environmental or social causes (Redfield, 2022). As the sustainable debt market gains complexity, the market has been divided into activity- and behaviour-based products (ibid). The activity-based products are when companies invest in a specific environmental or social outcome or project, such as green loans or *use-of-proceeds* bonds (sustainable, green, social, transition) (see Table 1). Behaviour-based products are when companies link their debt to a financial component with a sustainability target, such as sustainability-linked loans (SLLs) or bonds (SLBs)(ibid). There are both principles for bonds and loans regarding being classified as sustainable. The International Capital Market Association (ICMA) creates principles for sustainable bonds. ICMA was founded in 1969 to promote the development of the international primary market for Eurobonds (ICMA, 2023b). However, over the years, they have grown to cover various aspects of the international capital markets, including primary and secondary market activities, market practices, regulatory issues, and market infrastructure (ibid). For example, they write principles to provide guidance and promote best practices in specific areas of the capital markets (ibid). The Loan Market Association (LMA) issues sustainable loan market principles. Since establishing the LMA in 1996, its key objectives have been to improve efficiency, liquidity, and transparency in the primary and secondary loan market in Europe and EMEA¹ (LMA, na.).

¹ The Middle East and Africa (EMEA)

2.3.2 Use-of-Proceeds Bonds

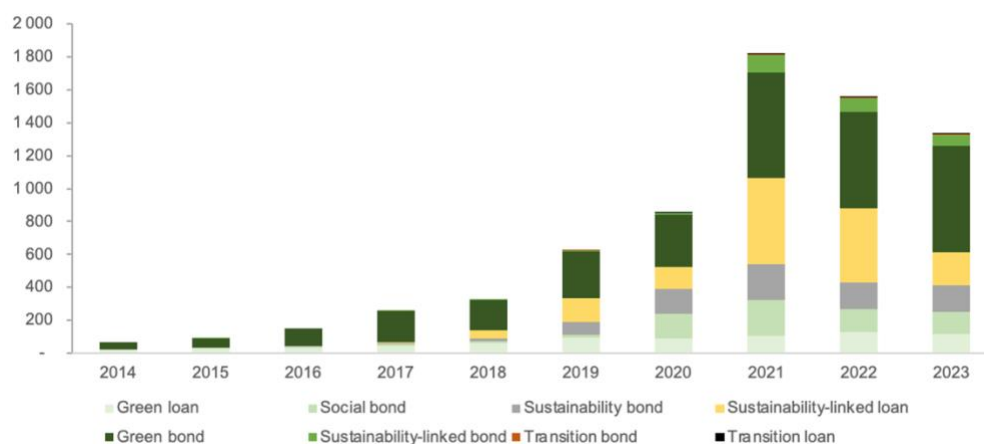
The share of sustainable bonds has increased significantly in the last few years, now representing 13% of the market and is anticipated to become 14% in 2024 (Cochelin et al., 2024). The sustainable bond market includes a variety of fixed-income instruments, including green, social, sustainable, and sustainability-linked bonds (GSSS-bonds) (see Table 1). Among these, green, social, sustainable, and transition bonds, categorised as *use-of-proceeds*, are explicitly issued to fund or refinance environmental or/and social projects (ICMA, 2023a). Green bonds dominate the sustainable debt market, comprising 48% of total issuance globally (see Figure 4). These bonds fund environmentally friendly projects, imposing constraints on companies' investment policies (Flammer, 2021).

Table 1
Overview of Sustainable Debt Categories

Activity-Based Products		Behaviour-Based Products	
Green Bonds	100% of proceeds used for eligible environmental activities 	Sustainability-Linked Bonds	General purpose debt: issuer commits to green and/or social targets 
Social Bonds	100% of proceeds used for eligible social activities 		
Sustainability Bonds	100% of proceeds used for environmental and social activities 	Sustainability-Linked Loans	Any types of loan instruments and/or contingent facilities which incentivise the borrower's achievement of ambitious, predetermined sustainability performance objectives 
Green Loans	Any type of loan instrument made available exclusively to finance or re-finance, in whole or in part, new and/or existing eligible Green Project 		

Source: ICMA (2023), LMA (2023a), LMA (2023b)

Figure 4
Global Sustainable Debt Issuance (in billion dollars)



Source: BloombergNEF, Bloomberg Terminal

2.3.3 Sustainability-Linked Bonds (SLBs)

Unlike *use-of-proceeds*, SLBs are a recent addition to the sustainability debt market (ICMA, 2023a). SLBs are a unique bond category with dynamic financial and structural features dependent on an issuer's achievement of predetermined sustainability or ESG objectives. SLB proceeds are used for general purposes, allowing issuers flexibility in addressing sustainability challenges across their operations (ICMA, 2023a). As of 2023, global SLB issuance surpassed USD 67 billion, while total GSSS-bonds issuance was USD 1 trillion (see Figure 4).

According to the ICMA's Sustainability-linked Bond Principles (SLBPs)(2023), SLB issuers explicitly commit to enhancing sustainability within a defined timeframe, measured by Key Performance Indicators (KPIs) and assessed against Sustainability Performance Targets (SPTs). Observing the SLBPs, KPIs ought to be quantifiable, relevant metrics to the issuer's core operations and possess significant strategic importance. KPIs may cover social, governance, and environmental objectives, such as the number of female board members or a company's GHG emissions. The KPIs should be externally verifiable, transparently defined, and measurable to improve credibility.

The SLBP states that the SPTs should illustrate an enhancement in sustainability that goes beyond the typical "business as usual" path and be ambitious. The SPT is set for issuers to have a predefined timeline associated with each KPI. They should also be based on benchmarks, such as international targets or science-based scenarios. Additionally, it is recommended to externally verify the SPTs by a second-party opinion (SPO).

SLBs allow the characteristics of the bond, such as coupon rates, maturity, and repayment amounts, to vary based on the achievement of predefined SPTs linked to KPIs (Kölbel & Lambillon, 2022). In addition, issuers must report on KPI performance against SPTs, emphasising seeking independent external verification (ibid). KPIs are also included in the bond structuring documentation, used for coupon redetermination, and tested regularly (ibid). Currently, coupon ratchets are the most prevalent form of performance-based adjustments to SLB characteristics (Vulturius et al., 2024). The adjustment typically works so that if a company fails to achieve the criteria defined, the coupon rises by 25 bps (Kölbel & Lambillon, 2022). There are cases when the coupon may decrease if the KPI is attained. If several SPTs are achieved, the company will have several coupon step-ups (ibid). However, when SPTs must be achieved near the bond's maturity, issuers and investors may opt for performance-linked characteristics other than coupon ratchets.

2.3.4 Sustainable Loans

Sustainable loans encompass various financial instruments to advance ESG objectives within the financial sector. Among these are green loans, specifically for eco-friendly projects, and SLLs, which tie loan terms to sustainability performance metrics (LMA, 2023a; LMA, 2023b). Both green- and

sustainability-linked loans have principles that they follow issued by the LMA (ibid). Notably, SLL issuance has surged since 2014 compared to green loans (see Figure 4).

3. Literature Review

The following section introduces the literature review of the study. The section commences with a review of existing research on the primary drivers influencing fund managers in their portfolio management. Subsequently, it narrows the focus to examine the existing literature on the factors influencing fund flows into sustainable mutual funds. In particular, the potential correlations between sustainable mutual fund flows and financial performance, sustainability ratings and labels, differentiation, and reputation. However, this study focuses on Article 9 corporate bond funds and the motivations for fund managers to issue them, noting the limited research in this area. Furthermore, this study aims to contribute to the existing literature by investigating the implications of SLBs for Article 9 funds. Given the limited relevant literature on SLBs, this study will assess the border literature of GSSS-bonds, both from an investor and issuer perspective, to broaden the perspective with different stakeholder perspectives.

3.1 Fund Manager Motives

In the context of fund manager motivations, mutual fund firms commonly earn a fixed percentage (management fee) of assets under management (AUM) as compensation, incentivising actions that boost total fund assets (Chevalier & Ellison, 1997). As a result, fund flows and management fees represent the two avenues through which fund managers can augment their income (ibid). Adding to this, research by Dalmácio & Nossa (2004) indicates that such incentives can give rise to agency conflicts between fund managers and fund investors, as fund managers may prioritise strategies aimed at increasing AUM instead of dedicating time to active fund management aimed at maximising returns. Additionally, as the fund size expands, another potential agency conflict may emerge due to the increased complexity of managing a larger number of holdings, which limits the ability to conduct thorough analysis compared to managing a smaller portfolio (ibid).

3.2 Sustainable Mutual Funds Flows

3.2.1 Financial Performance

Factors influencing fund AUM have been investigated by studies, highlighting that past financial performance can be seen as one driver for mutual fund flows (e.g., Chevalier & Ellison, 1997; Berk & Green, 2004). Although past performance does not predict future fund performance, these findings persist (Berk & Green, 2004). This suggests that the potential outperformance of sustainable funds compared to conventional ones may have contributed to their appeal to fund managers, who are incentivised to take actions that increase AUM (Chevalier & Ellison, 1997).

Existing research has explored the expanding range of mutual funds explicitly designed with social responsibility mandates (e.g., Geczy et al., 2005; Bollen, 2007; Renneboog et al., 2008; Benson & Humphrey, 2008; Renneboog et al., 2011; Bialkowski & Starks, 2016; Riedl & Smeets, 2017; Geczy et al., 2020), reflecting the increasing interest of fund managers in launching such funds. However, there is an absence of studies showing that sustainable funds outperform conventional funds. For example, Hartzmark & Sussman's (2019) findings suggest that sustainability positively predicts future performance but do not find evidence that high-sustainability mutual funds outperform low-sustainability mutual funds today (*ibid*). In line with this, additional literature shows that socially responsible mutual funds do not earn significant excess returns and that the performance of such mutual funds is not statistically different from the performance of conventional mutual funds (e.g., Hamilton et al., 1993; Statman, 2000; Bello, 2005).

In previous studies comparing fund returns between Article 8 and Article 9 funds, Cosma et al. (2023) analyse performance during crises (COVID-19 pandemic and the Russia–Ukraine war) and find evidence that Article 9 funds (dark green) perform better than Article 8 (light green) and Article 6 (conventional funds), during these periods. However, this outperformance is short-lived, suggesting a lack of sustained performance. With the SFDR regulation in place, Article 9 funds are more constrained in their investment scope since they must have sustainable investment as their primary objective, while Article 8 funds only need to prioritise environmental or social characteristics (*ibid*). Building on this, traditional theories such as the Markowitz Portfolio Optimization Model, Black-Litterman model, and robust estimation theory can only achieve the tangency or optimal portfolio if you do not limit your investment possibilities. Conversely, imposing constraints on the portfolio, such as with Article 9 funds, can lead to diminished performance. This aligns with previous studies emphasising that every time a portfolio is constrained, its performance suffers (e.g., Rudd, 1981; Hall, 1986; Diltz, 1995).

In examining the correlation between historical fund performance and fund flows, Massa (2003) introduces a more nuanced perspective on driving fund flows. This study shows that while past returns play a role, fund flows are also influenced by non-financial factors, including the level of sustainability integration into the fund's policy. In line with Massa (2003), several other studies show how sustainability affects the return-flow relationship of mutual funds. For example, Bollen (2007) discovered that inflows into SRI funds are more responsive to previous positive returns than conventional funds and that outflows of cash from SRI funds show less sensitivity to past negative returns. Regarding net investor cash flows, the same study observes that the monthly volatility is typically lower in SRI funds. Benson & Humphrey (2008) and Renneboog et al. (2011) support these findings that traditional funds' net flows are more sensitive to past returns than SRI funds. This can be explained by the value of social and ethical attributes, mitigating the role of past negative performance on fund flows (*ibid*).

Riedl & Smeets (2017) confirm that investors tend to increase their investments in companies demonstrating ethical behaviour due to their preferences aligned with pro-social and pro-environmental norms and attitudes. Their study reveals that investors prioritise *social signalling* over expected returns when investing in socially responsible investment (SRI) funds, explaining why they are willing to accept higher management fees for such funds. However, they also find that investors anticipating underperformance in SRI funds are less likely to invest socially responsibly (ibid). This indicates that fund managers overseeing sustainable funds cannot overlook financial performance, as it appears to influence investors' decisions.

3.2.2 Sustainability Rating and SFDR Label

Moreover, studies show how sustainability ratings can positively affect fund flows (e.g., Ammann et al., 2019; Hartzmark & Sussman, 2019; Ceccarelli et al., 2024). Ammann et al. (2019) present the link between mutual fund flows and Morningstar's Sustainability Rating. They find evidence that investors reallocate money from low-rated funds to high-rated funds based on the *globe rating* in the first year after the rating's publication. Hartzmark & Sussman (2019) agree with these findings and find evidence that investors anticipate superior fund inflows from funds with high sustainability ratings. Moreover, Ceccarelli et al. (2024) have conducted a similar analysis with Morningstar's labels but with the Low Carbon Designation (LCD) label. This measures a fund's environmental performance based on the underlying portfolio holdings' exposure to fossil fuels and the portfolio's carbon risk score (ibid). The study results show that funds with the LCD label see significantly more fund inflows than those without the label (ibid).

Regarding Article 9 funds, Ferriani (2023) found that a fund with a higher Morningstar sustainability rating and being an Article 9 mutual fund significantly increases net capital inflow. Furthermore, the role of the fund name for capital flows can be explained by Scherer & Hasaj (2023), finding evidence that Article 9 funds attract significantly more fund flows, confirming the regulator's views that the SFDR label can channel capital flows into more sustainable funds. Becker et al. (2022) find that after SFDR was launched, the sustainability ratings went up for the impacted funds. Together, this indicates that the implementation of the SFDR effectively channels capital toward sustainable investment opportunities. This is consistent with Ghoul & Karoui (2021), suggesting that fund managers use sustainability-related names (green) to enhance fund flow.

In addition, the self-designation aspect of the SFDR regulation presents an opportunity for greenwashing in the sustainable mutual fund market, where fund managers can claim that they uphold greater sustainability efforts than in reality. In line with this, Scheitza et al. (2022) show evidence that the SFDR system is ambiguous and arbitrary, where many Article 9 funds do not meet the requirements. The results show that 63% of the Article 9 funds do not meet the outlined impact requirements, and only 8% of the funds in the sample can qualify as impact-generating investments.

3.2.3 Differentiation

Moreover, Kostovetsky & Warner (2020) use fund prospectuses to measure product differentiation and provide evidence on how funds differentiate from each other. Bonelli et al. (2022) build on this work and study product differentiation in the mutual fund industry. They show that funds perceived as lower quality (indicated by lower Morningstar ratings) are inclined to adopt a niche product design to appeal to a smaller investor base. Where they find that niche or “unique funds” are related to ESG issues. Conversely, higher-quality funds are more likely to embrace a broad product design for wider acceptance. This is built on the idea that uniqueness enhances market power, allowing distinctive funds to charge higher fees, and their fund flows have a lower sensitivity to low performance. This implies that funds with a lower initial rating could benefit from a strategic shift towards increased fund uniqueness.

3.2.4 Reputation

According to Chen & Lai (2010), reputation is another factor that can affect the fund flows of a mutual fund. The authors examine reputation stretching and its impact on fund managers and fund performance and find that reputable fund managers enjoy an advantage in increasing net fund inflow and enhancing fund returns. Furthermore, their study indicates that investors are more likely to allocate additional funds to a new fund when managed by a manager with strong prior returns. Thus, the study suggests a linkage between AUM, reputation, and investor expectations, as a strong reputation leads to increased investments and, consequently, higher AUM. Chen & Lai (2010) do not focus on sustainability; however, if combined with other research that points towards sustainability being important for reputation (e.g. a meta-analysis of Gomez-Trujillo et al., 2020), fund managers can employ these branding strategies to enhance their reputation, thereby attracting greater fund flows in the future.

3.3 Sustainable Bonds

Regarding the development of sustainable bonds, one can recognise that various factors influence stakeholders toward sustainable debt. This part is divided into two parts: the investor perspective and the issuer perspective.

3.3.1 Investor Perspective

According to Zerbib (2019), investors tend to increase their investments in bonds that align with their pro-social and pro-environmental norms and attitudes. Centering on SLBs, as this is the focus of this paper, there is limited research in general due to their recent emergence. However, an industry report by Natixis (2021) provides evidence that most global investment managers see SLBs as a fit in most investment strategies, including ESG integration strategies and green bond funds. However, the study also finds that investors are concerned about the greenwashing risk of SLBs due to their

lack of transparency (ibid). Vulturius et al. (2024) acknowledge the same issue when comparing green bonds with SLBs and emphasise that investors have less control and insights over how the proceeds of SLBs are used. On the other hand, punishment for failing to meet the predetermined ESG targets aims to incentivise the issuer to reach the SPTs. This is confirmed by Liberadzki et al. (2021), emphasising investors' preference for SLBs over other *use-of-proceeds* due to the distinct factor of an enforceable and direct financial incentive for issuers to achieve the identified SPTs. In contrast, green bonds only entail reputational risk as a safeguard. Although the article does not explicitly address the direct impact of this, it can be inferred that the availability of a monetary incentive, unlike in green bonds, reduces risk for investors and serves as a rationale for investing in SLBs. Despite this, an industry report argues that companies can put up easily achievable SPTs as SLBP does not have a specific definition of elements deemed significant or ambitious (Liberatore, 2021). Moreover, there is research on penalties for SLBs not stringent enough, which instead incentivises issuers to prioritise SPTs and sometimes even benefit from issuing an SLB even though they do not reach the sustainability targets (Liberatore, 2021; Kölbel & Lambillon, 2022).

3.3.2 Bond Issuer Perspective

The secondary focus centres on bond issuers' incentives for issuing GSSS-bonds. Several studies have been analysing green bonds and the existence of a green bond price premium (*greenium*), comparing the pricing of green and conventional bonds, with varied results (e.g., Baker et al., 2018; Karpf & Mandel, 2018; Zerbib, 2019; Larcker & Watts, 2020; Flammer, 2021). Larcker & Watts's (2020) findings suggest that methodological design misspecification is the primary explanation for these varied results. Karpf & Mandel (2018) and Baker et al. (2018) observe a *greenium* yielding eight and six basis points lower than conventional bonds, respectively. In subsequent studies, strict matching methods are used for each green bond to match a quasi-identical conventional bond of the same issuer. This results in a slightly significant *greenium* (Zerbib, 2019) or no *greenium* (Larcker & Watts, 2020). However, most of the research focuses on municipal bonds due to their distinctive institutional characteristics (e.g., Baker et al., 2018; Karpf & Mandel, 2018; Larcker & Watts, 2020). Flammer (2021) contributes to this literature by conducting a detailed analysis of corporate green bonds and finding no observable *greenium*, which aligns with Larcker & Watts (2020).

Regarding existing literature analysing potential price premiums for SLBs, Kölbel & Lambillon's (2022) study finds that issuing an SLB yields nine basis points lower on average than a conventional bond. However, the bond issuer's first SLB seems to have a more significant premium, suggesting that investors especially see the first SLB as a credible signal of a firm's sustainability commitment. Moreover, this study emphasises that the penalty associated with failing to reach a target is relatively small and, in various cases, smaller than the savings for SLB issuers from the reduced cost of debt. This implies that SLB issuers can enjoy a "free lunch," meaning a financial benefit for bond issuers despite not achieving the target (ibid).

Moreover, Berrada et al. (2022) highlight the circumstances in which an SLB contract exhibits incentive compatibility and conclude that companies may issue SLBs to signal their dedication to sustainability credibly. Kölbel & Lambillon (2022) further align with the insights of Berrada et al. (2022), proposing that SLBs act as signalling tools for issuers. Moreover, these findings align with similar observations made by Larcker & Watts (2020) and Flammer (2021) in the context of green bonds, suggesting that companies use green bonds to communicate and emphasise their dedication to environmentally and socially responsible practices.

In addition, previous research suggests that bond issuers may decide to issue SLBs instead of *use-of-proceeds* from a financial point of view, implying that KPIs can be manipulated due to asymmetric information between investors and bond issuers (Barbalau & Zeni, 2021). Firms can raise funds using *use-of-proceeds* bonds but not commit to green outcomes, while SLBs do not impose restrictions on the *use-of-proceeds* but embed contingencies which incentivise commitment to outcomes. Hence, green bonds correct for moral hazard by adhering to a *use-of-proceeds* principle, which ensures credible commitment but gives rise to an *opportunity cost* of committing to projects before learning their green outcome potential. SLBs eliminate this *commitment cost*, but to the extent that the measurement systems on which contingencies (KPIs) are based can be manipulated are affected by a distortion discount. Consequently, in situations with asymmetric information about firms' integrity and willingness to fulfil commitments, low-type (smaller yet more polluting) firms may choose SLBs to exploit opportunities for manipulation, thereby avoiding the commitment cost that comes with *use-of-proceeds* (ibid).

3.4 Summary of Literature Review

Existing literature does not find that sustainable mutual funds outperform conventional ones (e.g., Hamilton et al., 1993; Statman, 2000; Bello, 2005; Hartzmark & Sussman, 2019). Regarding Article 9 funds, a research gap exists, with only one study indicating a brief period of outperformance during a crisis, suggesting a lack of sustained performance (Cosma et al., 2023). The absence of evidence supporting outperformance can negatively impact fund flows, posing a challenge for fund managers who are incentivised to implement strategies that increase AUM (e.g., Chevalier & Ellison, 1997; Berk & Green, 2004). However, we find that literature highlights other non-financial factors correlating with positive fund flows, for example, sustainability consideration (Massa, 2003), sustainability ratings (e.g., Ammann et al., 2019; Hartzmark & Sussman, 2019; Ceccarelli et al., 2024), and reputation (Chen & Lai, 2010). Literature moreover shows that sustainable mutual fund flows can be less sensitive to past negative returns (e.g., Bollen, 2007; Benson & Humphrey, 2008; Renneboog et al., 2011; Bonelli et al., 2022). Focusing on addressing Article 9 funds, the literature indicates that the Article 9 label can enhance net fund flow (e.g., Ferriani, 2023; Scherer & Hasaj, 2023). However, we do not find previous research investigating Article 9 bond funds, noting the limited available literature on sustainable bond funds. Hence, this paper aims to examine fund

managers' decision-making process in opting to issue an Article 9 corporate bond fund over an Article 8 counterparty, clarifying the rationale behind such choices and evaluating the associated advantages and disadvantages. Additionally, we conduct a case study of Lannebo and their decision to launch a sustainable Article 8 bond fund instead of an Article 9 bond fund to see if their decision relates to previous literature. Despite the potential perception that Article 9 funds may be less appealing for fund managers to initiate due to the lack of outperformance, they have exhibited the highest quarterly flow growth rates among all fund types since 2021 (see Figure 2). Thus, our research contributes to the existing literature by delving into the underlying motivations for launching an Article 9 fund over an Article 8 fund and contributes to understanding the market implications of SFDR.

The decision to delve into the Article 9 corporate bond fund market allows for exploring a potential correlation between the sustainable bond market and Article 9 bond funds through a secondary research question. Given that SLBs are the latest inclusion in the sustainable debt market with limited research, it presents an opportunity to explore their implications on Article 9 bond funds. Existing literature highlights concerns about the flexible structure of SLBs, such as lack of transparency over the proceeds (e.g., Liberatore, 2021; Berrada et al., 2022; Kölbel and Lambillon, 2022; Vulturius et al., 2024). However, we are the first study to empirically investigate the implications of SLBs on Article 9 bond funds, to our knowledge.

4. Methodology

4.1 Research Design

The research questions of this thesis aim to understand the Article 9 corporate bond fund market and instruments employed within these funds, with a particular focus on SLBs. The research method is based on qualitative data to answer the first and second research questions, and a case study is used to get further insight into the decision-making process in issuing an Article 9 or 8 corporate bond fund, answering research question 3. This practical application aspect is needed, especially considering the limited research and quantitative data on Article 9 funds and SLBs. The limited data can be explained by the relatively few issued SLBs and the short timeframe since the first issuance (September 2019). Furthermore, the SFDR framework was launched in 2021, which is relatively recent. These factors, therefore, present challenges for conducting a quantitative analysis with an extensive sample empirical analysis. Utilising a qualitative approach, the study provides detailed and nuanced descriptions of the research questions, a level of detail that is difficult to attain with quantitative research methods (Ahrne et al., 2015).

The case study method has been favoured by multiple researchers, specifically in situations with complex real-life circumstances, where only the case methodology could establish causality (e.g., Eisenhardt, 1989; Dubois & Gadde, 2002; Siggelkow, 2007; Swanborn, 2010). The aim of

using a case study is to empathise a general theme by investigating a particular one (Denscombe, 2017). By studying Lannebo's *Sustainable Corporate Bond* fund through a case study, the thesis aims to present the effects of choosing an Article 8 corporate bond fund instead of an Article 9 counterparty. However, case studies have also been criticised for not being a proper scientific method due to lacking generalizable results (Yin, 2014).

4.2 Data Collection

The primary data for this thesis was collected from interviews and a survey. Interviews are used to achieve in-depth analysis of a complex business situation. The selection of interviews and the case framework is based on an intentional selection (Yin, 2014). The interviews were semi-structured; in other words, the main questions were prepared before the interview, and additional questions were formulated at the time of the interview to follow up on a specific subject (Merriam, 1994). The questionnaire was structured to begin with broader, more general inquiries, aiming to capture a holistic overview. Subsequently, it delved into more specific queries aligned with the research objectives, addressing aspects relevant to the existing literature and identifying knowledge gaps. Moreover, the main interview questions were sent to the interviewee at least one day before the interview to gain an effective interview. This framework facilitated guided interviews, ensuring a structured progression yet remaining flexible enough to capture the spontaneous nuances brought up by the interviewees. In addition, a survey was distributed to the Article 9 fund managers after the interviews to supplement and deepen the conducted conversations for more quantifiable results.

This report aims two-fold, focusing on understanding different perspectives of Article 9 and 8 corporate bond funds and the effects of SLBs in this market. Therefore, 15 individuals have been interviewed. Interviewees have primarily been selected based on the individuals' relevance as decision-makers. To gain valuable insight from different Article 9 funds and SLB experts, interviews have been conducted with various stakeholders, such as fund managers, investors, bond issuers, underwriters, and specialists. Additionally, interviews are conducted with fund managers at banks and independent asset management firms to explore potential variations in their responses on this matter. To develop a thorough understanding of the Lannebo case, we interviewed their fund managers and head of sales. This approach provided valuable insights into Lannebo's key clients' perceptions of the company and its *Sustainable Corporate Bond* fund. Offering perspectives beyond those solely provided by the fund managers of this fund. An overview of the interviewees can be found in Table 2.

The interviews took place from January until March 2024 and ranged between 30 and 60 minutes. Interviews were both held in person and online. The interviews were transcribed within 24 hours from the record material to retain impressions, and then both authors discussed them. All interviewees consented to respond to additional questions, a chance utilised in various instances to deepen the comprehension of a particular situation or gather supplementary data.

Table 2
Overview of Interviewees

Company	Interviewee	Title/Background	Dependency	Comments
Lannebo	Karin Haraldsson	Fund manager	Dependent	23 Jan, 50 min
Lannebo	Katarina Ponsbach Carlsson	Fund manager	Dependent	23 Jan, 50 min
Lannebo	Emelie Wallin	Head of third-party distribution	Dependent	18 Mar, 40 min
Handelsbanken	Karin Görransson	Fund manager	Dependent	1 Feb, 60 min
Handelsbanken	Klas Wennerstein	Fund manager	Dependent	7 Mar, 45 min
ODIN	Nils Hast	Fund manager	Dependent	23 Feb, 50 min
Norron	Jan Törnstrand	Fund manager	Dependent	13 Mar, 50 min
Norron	Peter Werleus	Fund manager	Dependent	13 Mar, 50 min
Norron	Elin Carlberg	ESG Analyst	Dependent	5 Feb, 45 min
Swedbank	Lucas Rintala	Analyst, Sustainable Capital Markets	Independent	9 Feb, 30 min
PwC	Sophie Nachemson-Ekvall	Expert social sustainability, reporting and financing	Independent	23 Feb, 30 min
Swedish Investment Fund Association	Fredrik Nordström	CEO, Swedish Investment Fund Association	Independent	29 Jan, 60 min
KVA	Karin Forseke	President, Investment Committee	Independent	5 Feb, 60 min
Standard and Chartered Bank	Alexis Neilsen	Associate Director	Independent	19 Feb, Written
Bonava	Peter Wallin	CEO	Independent	8 Mar, 45 min

Complementary data, in addition to interviews and the survey, have been used. This data helped to challenge statements and ask follow-up questions during the interview sessions. The public data includes both secondary and tertiary data collected from industry reports and data providers. Examples of this are the fund's fact sheet, press releases, monthly reports, and data from the Swedish Investment Fund Association, Morningstar, S&P, and Bloomberg. A list of public data sources can be found in the references section.

4.3 Research Quality

One concern is that the case study methodology constrains the possibility of generalising results (Abercrombie et al., 1994; Yin, 2014). The validity of the research should be analysed through three different methods: internal, external and construct (Yin, 2014). Internal validity pertains to causality and holds particular significance in a case study context, given that researchers rely on shared information (ibid). Using multiple sources increases internal validity and addresses biases. External validity is connected to whether the conclusions can be extended to a broader context (ibid). This is not a quantitative study; therefore, the data cannot attain statistical significance or be tested in an “out-of-sample” context. Instead, the generalisation hinges on the researchers’ ability to extrapolate results into a broader theory analytically. Thus, the results presented in this thesis can indicate the current views on Article 9 corporate bond funds, including SLBs’ part in the transformation in the Nordics. However, it is not possible to conclude a broader generalisation. Construct validity assesses the suitability of the interpretations derived from observations (ibid). To achieve elevated construct validity, information was obtained using multiple methods and sources, including interviews, a survey, and public and non-public data. Moreover, triangulation has been used to analyse the research question from various perspectives (McMillan & Schumacher, 2009).

Reliability pertains to whether the research method has been executed in a way that enables the study to be replicated, yielding consistent results (Saunders et al., 2012). Interviews are impacted by the setting in which they occur, specifically for semi-structured interviews; given the interaction between interviewers and interviewees, they undergo an impact or influence. Moreover, the information collected in the interview requires interpretation, which is greatly dependent on personal perspective. Therefore, to achieve high reliability and minimise this subjectivity, both authors have taken part in all interviews, and interviews have been recorded and transcribed within 24 hours after the interview. However, as the case study pertains to a singular event at a specific moment, interviewees may recall the event differently in subsequent analyses. These factors diminish the likelihood that replicating the study would yield identical results.

Research ethics can be defined as behaviours and standards guiding the researcher’s conduct towards those who are affected by the research (Saunders et al., 2012). To ensure this, all participants have been briefed on the thesis objective, and any confidential statements have been included solely with the individual’s explicit consent.

5. Key Drivers for Article 9 Corporate Bond Funds & SLB Implications

Throughout this section, the empirical results of the interviews will be presented. This qualitative study delves into the insights from interviews with Nordic fund managers and other corporate bond fund industry stakeholders. While this thesis addresses the viewpoints of Nordic fund managers, the interviewees not only manage Nordic funds but also European and Global funds. Hence, the study

results are applicable beyond the confines of the Nordic market, providing insights into the European and Global sustainable fund landscapes as well.

Two interviews were conducted with fund managers from banks (SHB, 1871), while three were conducted with fund managers from independent asset management firms (ODIN, 1990; Lannebo, 2000; Norron, 2010). All interviewed fund managers, except Lannebo, currently manage Article 9 corporate bond funds. This section focuses on the sample of fund managers managing either an Article 9 corporate (with “investment grade” credit rating focus) bond fund or an Article 9 *high-yield* corporate bond fund. Collectively, these funds are referred to as Article 9 corporate bond funds in this paper. Since *high-yield* fund managers seek lower-quality bonds with credit ratings below *investment grade* (see Table 3 for risk profiles), this paper aims to investigate any potential differences in their responses related to Article 9 corporate bond fund managers and SLB implications. Moreover, this study focuses on funds with AUM ranging from SEK 1700-4100 million, with Handelsbanken's *Hållbar Global Obligation* fund at the forefront. See Table 3 for an overview of the Article 9 funds in the sample for this qualitative comparison. The viewpoints of these fund managers, together with other stakeholders, will subsequently aid us in the case study of Lannebo in Section 6, examining their choice to opt for an Article 8 fund instead of an Article 9 fund.

Table 3
Overview of Article 9 Funds in the Sample

	Handelsbanken Hållbar Global Obligation	ODIN Sustainable Corporate Bond	Norron Sustainable Preserve	Handelsbanken Hållbar Global High Yield
Fund managers	Karin Göransson	Nils Hast och Mariann Stoltenberg Lind	Jan Törnstrand och Peter Werleus	Klas Wennerstein
Year issued	2019	2022	2011	2022
Geographical focus	Global	European	Nordic	Global
Sustainability Rating (Morningstar)	4/5	4/5	4/5	4/5
Return 1 year (2024- 04-09)	3.1%	5.8%	6.9%	7.8%
AUM (SEKm, 2024- 03-31)	4053.0	1740.2	3153.9	2230.8
Management fee	0.2-0.5%	0.2-0.4%	0.3-0.8%	0.3-0.95%
Risk	2/7	2/7	2/7	3/7

Source: Morningstar, fund fact sheet

As previously noted in Section 4.2, this thesis further includes the perspective of investors, bond issuers, underwriting banks, and specialists. Analysing the perspectives and incentives of each key stakeholder aims to expand the understanding of the driving forces behind the rising prominence of sustainability in the corporate bond market.

5.1 Background: SFDR Implications

SFDR aims to increase capital flow into sustainable investments (Swedish Financial Supervisory Authority, 2022). When asking the interviewees about this, they acknowledged that the implementation of SFDR regulation has improved *market transparency* and reduced *greenwashing* among FMPs, in line with its main objective:

“What we have said is that the entire SFDR is based on transparency and disclosure, so we are trying to be as transparent as possible” - Nils Hast, Fund Manager, ODIN, 2024

“It was very fluffy before this [sustainability regulations], and there was a greenwashing risk since it [sustainability classification] was so easy to gain. But then came the Taxonomy and SFDR, making sustainability more tangible” - Jan Törnstrand, Fund Manager, Norron, 2024

The limited risk for greenwashing is moreover explained by Norron, acknowledging that fund managers are the ones taking the sustainability risk. Given that regulatory requirements tightened with the implementation of the second level of SFDR in January 2023, demanding more comprehensive disclosure of ESG methodologies, sustainability risks, and impact in pre-contractual documents and periodic reports, it is acknowledged in the interviews that some fund managers chose to downgrade from Article 9 to Article 8:

“I have seen quite a few Article 9 funds that have been downgraded to Article 8. We’re the ones who take on the sustainability risks. We’re the ones who say they are sustainable, and if you have an incorrect process and claim it is an Article 9, then customers can sue us” - Peter Werleus, Fund Manager, Norron, 2024

However, while the SFDR aims to increase market transparency and limit greenwashing, fund managers acknowledge that the self-labelling categorisation of Article 8 and Article 9 has also garnered significant attention. The SFDR framework allows fund managers to differentiate funds according to varying levels of sustainability ambition, presenting opportunities for them. These factors underlie the motivations driving fund managers to launch Article 9 corporate bond funds, which are explained in detail in Section 5.2 below:

“When SFDR came, you can then categorise these types of funds into Article 9 and Article 8. Absolutely, it significantly facilitates matters for fund companies” - Klas Wennerstein, Fund Manager, SHB, 2024

5.2 Key Drivers Behind Issuing Article 9 Corporate Bond Funds

Table 4 below provides an overview of all the determinants raised during the interviews and a complementary survey regarding the key considerations for launching an Article 9 corporate bond fund.

Table 4
Overview of the Key Drivers Discovered by the Interviewees

	SHB Hållbar Global Obligation	ODIN Sustainable Corporate Bond	Norron Sustainable Preserve	SHB Hållbar Global High Yield
Differentiation opportunities	✓		✓	✓
Regulatory pressure	✓	✓	✗	✓
Client demand (fund flow)	✓	✓	✓	✓
Supply of compliant bonds	✓	✗	✗	✗
Performance		✗	✗	
Greater impact while lower volatility than Art. 9 equity funds		✓		✓

(Green=key driver, Grey=partly a driver, Red=not a driver)

5.2.1 Differentiation Opportunities and Pressure from SFDR Labelling System

The implementation of SFDR has prompted fund managers to identify new business opportunities in the form of a more niche fund type (Article 9) with higher sustainability commitments. In line with this, the CEO of the Swedish Investment Fund Association (Nordström, 2024) expects the future market for Article 9 funds to grow given their niche and clear impact goals. The interviews reveal that launching Article 9 corporate bond funds has been attractive for fund managers to differentiate from Article 8 counterparts. This is particularly notable considering that Article 9 funds comprise 6% of the fund market (see Figure 3). The *strategic differentiation* is acknowledged to be crucial for certain fund managers to reduce market competition and gain market share:

"We saw that there were fewer [Article 9] funds in that market. The other thing we hoped for was less competition and then the opportunity to gain market share" - Peter Werleus, Fund Manager, Norron, 2024

"All fund managers want to be seen as offering the most cutting-edge products, so an Article 9 fund is indeed considered to be the epitome of sustainability. And no one wants to admit they're lacking in sustainability either" - Klas Wennerstein, Fund Manager, SHB, 2024

Moreover, we observe that some fund managers surpass mere fund differentiation by incorporating an additional layer by expanding the geographical scope of Article 9 corporate bond funds. Not all fund managers possess the capability or resources to adopt a broader geographical focus, so this strategy inherently stands out. Several interviewees pointed out that despite the substantial growth of sustainable bonds, diversified, sustainable investment is insufficient for Article 9 bond funds in the Nordic market. When asked about the rationale behind launching an Article 9 corporate bond fund with a broader geographical mandate, fund managers posit that it serves fourfold purposes: achieving greater risk diversification, bolstering the fund's differentiation from peers, greater liquidity, and flexibility. It reaffirms that fund managers are actively seeking differentiation in their product offerings, and Article 9 corporate bond funds have proven to be a suitable target for accomplishing their mission. However, the limited possibilities in the Nordics call for a need for global scope for diversification:

“Handelsbanken chose to create a global Article 9 corporate bond fund to stand out a bit from many of its peers” - Karin Göransson, Fund manager, SHB, 2024

“If you take a Nordic mandate, you get a lot of Swedish real estate companies, which can be either good or bad. But I think when the upside is limited, I prefer to buy some other sectors as well, and we can achieve that with a European mandate” - Nils Hast, Fund manager, ODIN, 2024

“But of course, to achieve good risk diversification in these Article 9 funds, it's good to have a global mandate” - Klas Wennerstein, Fund Manager, SHB, 2024

In addition, fund managers acknowledge that increased market transparency from SFDR offers a chance for fund differentiation and introduces *regulatory pressure*. This can be explained by the extent to which a fund contributes to sustainability, which has to be disclosed (Articles 6, 8, 9) and can therefore impact a fund's reputation. This increases regulatory pressure on fund managers to be more sustainable. When questioned about this, fund managers rated regulatory pressure from SFDR and the EU Taxonomy on average as 3 on a scale of 5 as a driving factor for launching an Article 9 fund (see Appendix 7). This aligns with an ESG-bond underwriter analyst (Lucas Rintala, 2024), confirming that SFDR and the EU taxonomy not only build possibilities but also pressure fund managers to choose sustainable options.

While we see that the new EU sustainability regulations have a role in facilitating transparency in the sustainable fund landscape, these regulations are still relatively new to the market. Hence, acknowledged challenges remain within the EU regulation system, and one example is the data collection problems. Managing an Article 9 fund entails significant data collection and administrative effort to ensure transparency. This suggests that challenges for Article 9 funds remain, which may explain their relatively small market share compared to Article 8 funds:

“The entire field of sustainability management is still considered very new, and we have come a long way [...]. But new challenges keep emerging all the time. Especially this data collection” - Klas Wennerstein, Fund Manager, SHB, 2024

5.2.2 Demand from Institutional Clients

Interviewees are acknowledging a notable increase in demand for sustainable investments, driving the issuance of new Article 9 bond funds:

“We saw a greater interest and awareness among our investors [clients], and the market for green bonds grew quite significantly” - Karin Göransson, Fund manager, SHB, 2024

“We have indeed seen a much greater demand for sustainable investments globally [...]. Even last year, there were plenty of flow reports; while the general flows were negative in the market, it was still positive in certain sustainability-related funds, and this has also come with the fact that the whole world has become much more aware that we need to transition” - Elin Carlberg, ESG Analyst, Norron, 2024

As seen in Figure 2, Article 9 funds have had the highest growth rate of all fixed-income fund types since 2021. This marks a surge in demand for sustainable investments, which has opened new opportunities for fund managers, as emphasised in the interviews. For example, ODIN has recognised that launching an Article 9 fund and attracting client attention has become more accessible due to the high demand for these funds. Unlike Article 8 funds, where a lengthy track record may be required to attract institutional investors - often around three years for an Article 8 fund - Article 9 funds can access investor interest earlier. This is attributed to the sustainability aspect of Article 9 funds, which prompts earlier dialogues and engagements with potential investors:

“Thanks to being an Article 9 fund, we manage to engage in numerous dialogues and discussions because there is a great interest and demand. This has turned out to be an extra benefit we were unaware of initially. So, for many, it provides us with the opportunity to access people without having that track record” - Nils Hast, Fund manager, ODIN, 2024

“I think selling it [Article 9] to customers is easier. It is not that they only go by the article now, but when it is an Article 9, you get fast-track to investors without having to define it” - Jan Törnstrand, Fund Manager, Norron, 2024

Moreover, fund managers are acknowledging a contrast between retail and institutional investors' preferences, highlighting that institutional investors are to a larger extent interested in their sustainable corporate bond fund than retail investors:

“There is not much in the retail class, which may be related to the fact that retail prefers to buy stocks and then keep the money in a bank account. [...] But for an institution, we only see more and more interest, I would say” - Nils Hast, Fund manager, ODIN, 2024

“Especially when you think about Preserve now, which is an Article 9 [fund], there are significantly more institutional investors, [...] they are very tough on us when it comes to sustainability” - Jan Törnstrand, Fund Manager, Norron, 2024

“We experienced pressure from customers, especially from larger companies or the larger institutional companies. They pushed and emphasised that this [Article 9] is an interesting angle and would be good if we do it” - Jan Törnstrand, Fund Manager, Norron, 2024

One explanation for higher client demand among institutional investors is related to the fact that many of them have committed to various emission reduction goals and participate in different sustainability initiatives, such as the net-zero-asset-owner initiative. Consequently, investors feel compelled to invest sustainably or even opt to exclude certain investments to meet these sustainability requirements:

“Many investors also have committed to various emission goals and are involved in various initiatives. Yes, but there are initiatives like the net-zero-asset-owner initiative and similar ones, and then they are also forced to invest sustainably or even choose to exclude certain investments” - Lucas Rintala, Analyst Sustainable Debt Markets, Swedbank, 2024

In addition, an interviewed institutional investor (Forseke, 2024) highlights reputational risk and business risk related to not being committed to sustainability. Forseke acknowledges that institutional investors are afraid of getting involved in scandals and, hence, face more pronounced reputational risks. This could be an additional potential explanation for why institutional investors demand sustainable mutual funds, such as Article 9 corporate bond funds:

“Nobody wants to be involved in a scandal [...]. It is not just a reputational risk associated with an investment that has caused harm. [...] You also expose yourself to greater risks, business risks” - Karin Forseke, Chair of the Investment Committee, KVA, 2024

Finally, to better understand to what degree the increased demand for sustainability from clients (retail and institutional), resulting in increasing fund flows, has influenced the decision to launch Article 9 funds, the fund managers were asked to rank its importance. On average, fund managers see client demand as 4 on a scale of 5 as a driving factor in launching an Article 9 corporate bond fund (see Appendix 7).

5.2.3 The Role of Banks and Bond Issuers

Beyond fund clients, other stakeholders influence the development and expansion of Nordic bond fund managers' issuance of Article 9 corporate bond funds. Banks are implementing transition plans with specific targets for the proportion of bonds they underwrite to be GSSS-formatted. This shift is driven by internal rules implemented by banks to mitigate risks in the future (Rintala, 2024).

Moreover, bond issuers recognise that aligning with sustainability standards is essential to secure debt financing, thus increasing the availability of GSSS-bonds (as seen in Figure 4) and indirectly fostering a broader Article 9 market.

Banks

The interviews show that banks actively promote the issuance of GSSS-bonds among their clients whenever feasible. This initiative stimulates the supply of GSSS-bonds in the market. A bond underwriter at Swedbank mentions the bank's new transition plan, aiming for at least 40% of the bonds they arrange to be GSSS-formatted by 2027. This goal requires them to boost the proportion of GSSS-bonds. They assess customers' green assets and may recommend a *use-of-proceeds* format. If not available, an SLB is suggested:

“Now, in January, the bank communicated outward such a transition plan [...] by 2027, at least 40% should be ESG-formatted [GSSS-formatted], so it's a goal that affects us as well because we have to work to increase the proportion of ESG bonds [GSSS-bonds]. And yes, we work with it in such a way that if we see that the customer has enough green, social, or sustainable assets, one can recommend a use-of-proceeds format, and if they don't have it, then a sustainability-linked format can be an alternative” - Lucas Rintala, Analyst Sustainable Debt Markets, Swedbank, 2024

Bond Issuers

From a bond issuer perspective, the CEO of the Swedish residential development firm Bonava (who currently has an outstanding green bond in the market) highlights the evolving perception of sustainability, noting that it has shifted from being a future-oriented consideration to a hygiene factor (Wallin, 2024). A significant catalyst behind this shift is EU regulations such as the Taxonomy and CSRD, which enforce entities to adopt sustainability standards. Consequently, prioritising sustainability has become imperative for all entities. Those failing to do so risk being declined financing, jeopardising their survival in the market:

“I believe sustainability has transitioned from being something beneficial for the future to becoming a hygiene factor today. The stakes are raised further with the EU Taxonomy, as everything is compelled to adhere to it in a different manner, which indeed brings this into focus” - Peter Wallin, CEO Bonava, 2024

Therefore, banks and bond issuers play a role in expanding the market for GSSS-bonds, thereby facilitating the availability of sustainable investments suitable for Article 9 corporate bond funds. This is crucial for launching such funds, considering their niche nature and limited investment scope. However, investment opportunities remain restricted, which still limits the possibilities for the broader expansion of Article 9 funds:

“Generally speaking, there's a bit less, or there's less variety [of bonds] when it comes to Article 9” - Jan Törnstrand, Fund Manager, Norron, 2024

This explains why the Article 9 corporate bond funds market remains small today. As mentioned, a restricted variety of GSSS-bonds in the Nordics constrains the total amount of Article 9 bonds issued.

5.2.4 Financial Returns Interplay of Article 9 Bond Funds

Fund managers do not perceive superior performance in Article 9 corporate bond funds compared to Article 8 counterparties today. Hence, when examining the rationale behind starting an Article 9 bond fund and the relationship with financial returns, it becomes evident that fund managers do not expect higher returns from these funds. Instead, a challenge lies in a narrower investment universe for Article 9 funds, which do not enable the same opportunity to yield comparable returns to Article 8 bond funds, according to fund managers.

While Article 9 corporate bond funds encounter challenges in achieving comparable returns to Article 8 corporate bond funds due to their narrower investment scope, fund managers emphasise that the Article 9 label offers other appealing factors. One perspective argues that Article 9 bond funds can serve a broader purpose than solely maximising fund returns, reducing pressure on fund managers. Norron and ODIN emphasise that for many fund investors who invest in Article 9 funds, sustainability commitment can outweigh financial returns in importance:

“Customers are a little more forgiving if slightly lower returns exist. Not everyone, but for some customers, I think it has become quite important that it is an Article 9 fund” - Jan Törnstrand, Fund Manager, Norron, 2024

“However, the advantage of Article 9 is that customers have chosen it because they know they might sacrifice some return for investing correctly. [...] if I narrow down the universe, all else being equal, I should not have the same opportunity for good returns. But at the same time, I consider that these companies might be less likely to default” - Nils Hast, Fund Manager, ODIN, 2024

“Once we have gone through all these tests and reviews, I still think the fund becomes a little more attractive, a little more forgiving if it performs slightly worse than peers or something similar” - Jan Törnstrand, Fund Manager, Norron, 2024

In contrast to the discussion above, several interviewees argue that one cannot allow for lower expected returns because it is an Article 9 fund. This is built on the idea that sacrificing financial performance ultimately undermines the long term sustainability of investments:

“I do not think it [lower returns] is sustainable in the long run. All companies will need to undergo some form of sustainability journey, so an Article 9 fund must offer income and returns comparable to non-Article 9 funds. Returns are crucial, I believe, going forward for all investment products” - Klas Wennerstein, Fund Manager, SHB, 2024

In line with this, the issuer side (Wallin, 2024) acknowledges that being the first mover in sustainability can serve as a value to the fund managers; nevertheless, in the long run, investors typically prioritise funds with superior returns, reflecting the dynamics of the market economy. Hence, over time, possessing an Article 9 fund that does not perform at the level of an Article 8 or 6 fund of equivalent creditworthiness will not give any advantage. Therefore, the financial performance of Article 9 funds is not considered a less critical factor than other funds.

In summary, fund managers do not anticipate higher expected returns from managing Article 9 corporate bond funds than their Article 8 counterparts in the short term. However, on average, financial returns remain an important consideration for Article 9 bond fund managers, as evidenced by Appendix 7. Hence, the attractiveness of launching Article 9 corporate bond funds risks diminishing unless these funds yield comparable returns to Article 8 and Article 9 funds in the long run.

5.2.5 Article 9 Bond Funds vs Equity Funds

Examining the fundamental reasons for fund managers' issuance of Article 9 corporate bond funds reveals distinctions from Article 9 equity funds, extending beyond risk and return dynamics considerations. According to statements from multiple interview participants, debtholders have a more significant and swifter influence over portfolio companies than shareholders. The reason is that it is crucial for portfolio companies to get their bonds refinanced so that they can continue operating. Hence, Article 9 bond fund managers can push for sustainability initiatives to a larger extent than Article 9 equity funds, as the fear of not securing debt financing prompts portfolio companies to align with fund managers' interests:

“A company, a bit drastically, they do not care about who owns the share. [...] However, on the other hand, the bonds need to be refinanced every third to fifth year, and then we can raise the requirements we set. So, if we own a bond, the green framework should be updated, and so on. Then we have the opportunity to set more and stricter requirements than shareholders, which allows for progress in development” - Nils Hast, Fund Manager, ODIN, 2024

“In the bond market, many argue that there are more opportunities to impose requirements on companies, [...] But if a significant portion of investors no longer wants to buy the bonds, many emphasise that bonds have a significant potential for influence, actually more than to vote” - Fredrik Nordström, CEO, Swedish Investment Fund Association, 2024

“I believe that shareholders can vote on things and influence in that way. Absolutely. At the same time, on the credit side, we can choose not to lend money, which immediately becomes tough for companies. The other [equity] is a slower process” - Klas Wennerstein, Fund Manager, SHB, 2024

Furthermore, a fund manager acknowledges the benefits of GSSS-bonds by emphasising the risk associated with investments in stocks with high ESG ratings. This is due to a market where valuations of ESG stocks have surged and then crashed, as a result making ESG bonds a better alternative in terms of risk:

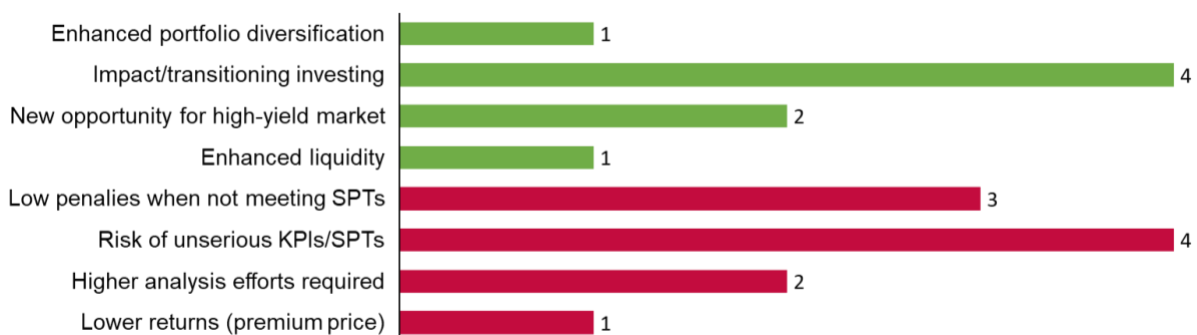
“We can see that on the equity side, valuations have kind of skyrocketed, and there has been a bit of a backlash. I believe that in the past 12 months, everything with ESG in its name has not fared well. Here, the advantage, I would say, lies with the bond side, speaking from my perspective. The thing is that valuations never skyrocket because I would never buy a bond with negative interest. I would not buy a bond where I get paid less than in, for example, a Swedish government bond. So, it means there is a limitation on how much valuation can go off. Therefore, there has been a better development” - Nils Hast, Fund Manager, ODIN, 2024

Therefore, a driver for Article 9 corporate bond funds lies in their potential to deliver a more significant impact while offering a safer and less volatile investment option than Article 9 equity funds.

5.3 SLB Implications on Article 9 Bond Funds

Figure 5 below provides an overview of all the factors discussed in the interviews, considering the advantages (green) and disadvantages (red) of SLBs according to fund managers interviewed.

Figure 5
Overview of the Advantages and Disadvantages of SLBs for Article 9 Bond Funds Identified by the Interviewees



5.3.1 Enhanced Portfolio Diversification Through Transition Investing

According to interviewees, the flexible structure of SLBs results in issuers from a wide range of industries being able to issue them. This enables fund managers to achieve a more diversified portfolio, according to Lannebo:

“You can get a diversified portfolio more easily if you include SLBs. And that is where SLBs come in for us” - Katarina Ponsbach Carlsson, Fund manager, Lannebo, 2024

Moreover, SHB explains that while large companies with established assets can issue green bonds, such as real estate firms, SLBs offer an opportunity for other types of companies with smaller balance sheets or those that want to transition to become more sustainable to align their financing with specific climate goals. Moreover, fund managers argue that some bonds labelled as green may not provide substantial benefits. This suggests that SLBs, with the right KPIs, can have a more significant impact or additionally than *use-of-proceeds*:

“Large companies with fixed assets can somehow always issue green bonds, but there are other types of companies, maybe those with smaller balance sheets or companies that want to transition. An SLB is a great opportunity for them to align their financing with predefined climate goals. And in a way, I think that an SLB with the right KPIs can have more impact and improvement than what a green bond might achieve in some cases” - Karin Göransson, Fund manager, SHB, 2024

“I am convinced that many SLBs bring about more significant changes in companies than most green bonds” - Klas Wennerstein, Fund Manager, SHB, 2024

Moreover, ODIN is expressing support for a shift in investment focus from seeking perfection to prioritising transitional investments that can make a meaningful impact. Similar to SHB, ODIN furthermore highlights that while green bonds are more accessible to finance for companies with operations conducive to such bonds, it is challenging for companies with integrated business models to establish green frameworks. This makes the SLB instrument an opportunity for companies in all business models to implement transition programs with defined KPIs, predicting a substantial increase in SLB adoption as a result:

“One has transitioned from investing in what is perfect to investing in transition where one can really make a difference. I think that is great because obviously, everything that's perfect does not necessarily need my money [...]. Green bonds presuppose that the company has a business that can be packaged as a green bond, but for other companies that are very integrated, it is much harder to create green frameworks. SLBs emerge as an opportunity to set up a program for transition then and have KPIs to be met and so on [...]. That is why I think SLB will increase significantly” - Nils Hast, Fund Manager, ODIN, 2024

An independent interviewee adds that companies issuing SLBs and SLLs tend to be better at general sustainability work and sustainability reporting, which increases value for investors due to improved transparency. This can also be linked to the transformation of companies, with sustainability-linked attributes facilitating the transition of firms toward greater sustainability:

“It becomes transparent in a completely different way, and that is what I have seen when I have looked at 63 real estate companies and found about fifteen of these loans. However, both SLL and SLB report what they do; they are also much clearer in their reporting in the annual reports and on the Taxonomy. They are better at setting internal goals and are extremely prepared for sustainability reporting, CSRD. It creates strategy, value for the company, and value for the investor collective. So, it is more than just this bond framework” - Sophie Nachemson, Expert Social Sustainability, Reporting & Financing, PwC, 2024

This suggests that the rising popularity of SLBs can be attributed to their flexible structure, which allows firms from various industries to issue them, thereby facilitating fund diversification. Notably, SLBs offer smaller companies and those in transition opportunities to align financing with climate goals. SHB advocates this shift towards transitional investments, with ODIN also predicting a significant increase in SLB adoption. Additionally, insights from a sustainability expert confirm that SLBs enhance transparency and investor value, further supporting these findings.

5.3.2 Greenwashing Risk

Investigating the challenges of integrating SLBs in Article 9 corporate bond funds, the interviews indicate that SLBs are currently not the ideal bond type for inclusion in these funds due to challenges and concerns regarding the greenwashing risk. Firstly, the interviewees bring up instances where KPIs and SPTs were either too easy to achieve or too vague. In addition, fund managers argue that the penalties for not meeting SLB targets are minimal, increasing the risk for fund managers investing in companies that do not meet the SLB targets or set SPTs they have already reached. As a result, many fund managers avoid SLBs, which helps explain the relatively low prevalence of SLBs compared to *use-of-proceeds* bonds in Article 9 corporate bond funds today:

“There have been cases with SLBs where we found the KPIs were either too easy to achieve or too vague. So far, the penalties for this have been quite small. Maybe you raise the redemption price from 100 to 100.5 or 101. It is not like it will seriously harm the company, and it will not dramatically affect our returns. If this is supposed to make a big difference for investors, then maybe you have to raise the bar there” - Katarina Ponsbach Carlsson, Fund manager, Lannebo, 2024

“But with SLBs, you must also be very careful and check that the KPIs are essential for this company's sustainability efforts. You have to read them with a very critical eye when going through them” - Karin Göransson, Fund manager, SHB, 2024

“My concern, or the problem I still see with it [SLBs], is that I think there is a risk of greenwashing. SLBs should have KPIs on various sustainability goals, and for me, it is tough to determine if these are ambitious KPIs or just a walk in the park” - Nils Hast, Fund manager, ODIN, 2024

“We think the penalty is too small [for SLBs]” - Jan Törnstrand, Fund manager, Norron, 2024

“Some of these goals [SPTs] have already been achieved, that is how it is. Then it is [the SLB is] just for marketing purposes, but now we should not generalise everyone; there are exceptions. There's a certain cynicism in the market that not everything is just for good” - Peter Werleus, Fund Manager, Norron, 2024

Looking at the penalty for SLBs failing to achieve their defined SPTs, an interview with an Associate Director at Standard Chartered Bank (Nielsen, 2024) confirms the fund managers' statement that it is more of a reputational risk issue than a cost issue if they publicly do not meet their targets.

Nevertheless, regarding the future potential growth of the SLB market, several fund managers express optimism. This is based on the expectation that SLBs will become more standardised and regulated, particularly with the guidelines provided by ICMA. Fund managers emphasise the importance of selecting comparable KPIs across companies issuing SLBs to facilitate meaningful comparisons. The main goal of SLBs should be to encourage companies to set ambitious targets rather than maintaining the status quo, emphasising the need for continuous improvement and effort. Furthermore, the future coupon rates are developing, and we will see where new directions will land:

“I believe that it will become more streamlined, and now we have ICMA, which has provided guidelines on what an SLB should contain to establish some kind of market practice. I think the most important thing is to choose similar KPIs to compare between companies so that we do not create some homemade KPIs with no idea how to compare with another company in the same sector, for example. Because the most important thing for an SLB is that there is an ambitious path. It should not be business as usual; they must strive for progress” - Karin Göransson, Fund manager, SHB, 2024

Moreover, the SPOs are essential for the future. To make SLBs and their KPIs and SPTs as reliable as any other bond, one will need to have supervisors and legislation over the SPOs, similar to what there is today with the credit rating companies such as Moodys and S&P:

“I do not know if more regulatory efforts are needed. It is more that we, as investors, also demand these second opinions. I mean, there is a framework and then comes a second opinion” - Klas Wennerstein, Fund Manager, SHB, 2024

Despite challenges, the SLB market holds significant growth potential. Effective management of these challenges, such as streamlining reporting processes, ensuring standardisation

of KPIs, and increasing penalties if issuers do not meet the predetermined SPTs, could further expand the SLB market. As investors tackle these obstacles, the SLB market will become more transparent, and the risk of greenwashing will decrease. Hence, there is optimism that Article 9 corporate bond funds will increase their exposure towards SLBs in the future.

5.3.3 Higher Analysis Efforts

Another challenge and concern regarding SLBs is the comparatively higher analysis effort required compared to *use-of-proceeds* bonds. The SLB structure depends on an issuer's achieving predetermined sustainability objectives, offering *flexibility* in addressing sustainability challenges across firm operations. Their flexible structure results in SLB proceeds being typically used for general purposes (ICMA, 2023a), raising fund manager concerns about whether to classify them as sustainable investments. Hence, to include SLBs in Article 9 funds, fund managers argue that additional analysis needs to be conducted and that certain criteria must be met to ensure the SLB aligns with Article 9 bond funds' objectives. More specifically, fund managers acknowledge that managing SLBs requires as much effort as handling conventional bonds. They emphasise assessing the entire company before investing, ensuring a deep understanding and comfort level with all aspects of its operations. Therefore, it takes much time to find interesting sustainable companies such as SLB in which to invest. Unlike SLBs, *use-of-proceeds* are explicitly directed towards sustainable projects or assets, providing clear traceability of proceeds towards environmentally friendly initiatives such as green buildings. This can explain the small number of SLBs included in sustainable bond funds today compared to *use-of-proceeds*. Furthermore, given the availability of *use-of-proceeds*, this suggests that SLBs are not vital for initiating Article 9 corporate bond funds:

"We do not see them [SLBs] as a sustainable investment. However, to include them in our Article 9 funds, we have to do an extra analysis, and then we have to check quite a few boxes [...], which is why I have very few. I think I have 3 or 4 in the fund at the moment, and I do not think there will be much more because, in my world, there is still a lot to choose from in the use-of-proceeds format" - Karin Göransson, Fund manager, SHB, 2024

"One could say that just like with social [bonds], for SLBs, we should be comfortable with the entire company for SLBs to work. That is because you cannot track the proceeds in the same way as with green bonds. Later on, I think that will develop so that you might get greater differences and perhaps greater traceability of exactly what the SLB money is used for. Then, you could certainly consider SLBs from companies that may lean a bit more towards the brown side. But today, we want it to come from companies that are comfortable with them" - Nils Hast, Fund Manager, ODIN, 2024

However, an independent perspective from the Social Sustainability, Reporting, and Financing expert at PWC, Sophie Nachemson-Ekwall, criticises the negative arguments about SLBs for taking too much analysis effort. Nachemson-Ekwall argues that climate change needs to be

combated right away even if the additional time required for evaluating SLBs compared to investing in *use-of-proceeds* or conventional bonds, fund managers need to take action:

“I think all this about “it takes too much time”, I find it silly, and I think it is yesterday. We need to make a change” - Sophie Nachemson-Ekwall, Expert Social Sustainability, Reporting & Financing, PwC, 2024

These observations suggest that SLBs may not be the optimal bond type for inclusion in an Article 9 fund today. ODIN further acknowledges the challenges that SLB reporting poses for Article 9 bond funds, particularly emphasising the potential overload of reporting tasks. However, they remain hopeful that the situation will improve as more companies report and provide data. They further appreciate the efforts to enhance reporting transparency.

5.3.4 Potential SLB Greenium

We examine the pricing of SLBs to determine if this factor influences their inclusion in Article 9 corporate bond funds. There is no clear evidence of this in the interviewees as the answers are mixed and point towards the pricing being dependent on market conditions. The absence of evidence for a *premium* implies that it neither hinders nor promotes SLBs' inclusion in Article 9 funds, suggesting no impact on Article 9 fund issuances. When asking about premiums, two independent interviewees state that they can see *greenium* for green bonds but are not certain it exists for SLBs:

“There is occasionally a greenium, and it is related to supply and demand [...] It is not the same when pricing a linked bond as when pricing a green bond. For a green bond, you have the greenium quite easily, but when it comes to an SLB, you practically get you also pay for the credit risk or for not delivering on what you have committed to, so there, I am not sure” - Sophie Nachemson, Expert Social Sustainability, Reporting & Financing, PwC, 2024

“We see it [premium pricing] especially in green bonds. The format, all types of EU formats [GSSS-bonds], can also have a new greenium, but it really depends on market conditions, so it is. It cannot be said that it is a static figure; it depends on market conditions” - Lucas Rintala, Analyst Sustainable Debt Markets, Swedbank, 2024

Moreover, ODIN emphasises an existing market premium for ESG bonds (GSSS-bonds) and prefers to invest in bonds without the “ESG label” from issuers they find sustainable. This strategy is expected to yield higher expected returns while prioritising sustainability. However, at the same time, acknowledging that ESG bonds may offer better liquidity during market downturns or uncertain times, making them easier to sell. Therefore, this suggests that it might be worthwhile to pay a premium for better liquidity, even if it means sacrificing some potential returns:

“The idea is that the company should have lower capital costs to issue an ESG bond than a non-ESG one, and that is why, in those cases where we like the company, we prefer to buy the non-ESG ones because we believe there will be a bit more return in them. At the same time, fund managers can think that liquidity is important, whether I have a green or a non-ESG one, and in times of market downturns or uncertainty, it's probably much easier to sell the green one than the non-green one. So, it might be worth paying a little for better liquidity” - Nils Hast, Fund Manager, ODIN, 2024

In contrast, the CEO of Bonava (Wallin, 2024) represents an ESG issuer perspective and acknowledges that he has not seen an existing market premium. Instead, the crucial factor is whether there is access to capital, as it becomes more difficult to receive financing for companies issuing non-ESG bonds today. Hence, the question boils down to *who receives financing and not*, rather than a *lower cost of capital for sustainable companies*:

“In your questions lies the essence: is there any premium? I would like to say absolutely not. No, there is no premium; however, there is the availability of capital or not, so it is binary from that perspective rather than based on price” - Peter Wallin, CEO, Bonava, 2024

Like Bonava, Norron does not see a significant market premium for SLBs. Instead, they acknowledge a *brownium* in the market, suggesting discounted bond pricing for companies heavily reliant on fossil fuels or coal. This is reasonable as bonds issued by these companies likely face less demand from investors due to their negative environmental impact, resulting in a higher cost of debt.

In summary, interviewees hold varied perspectives on the existence of a premium for SLBs. While some perceive a slight premium of a few basis points, others have not yet observed any premium at all. From a pricing standpoint, a lower premium for SLBs compared to *use-of-proceeds* bonds could potentially enhance their attractiveness for inclusion in Article 9 bond funds. A lower SLB premium would enable fund managers to invest sustainably while obtaining more favourable pricing than *use-of-proceeds* bonds. However, our findings do not currently show this.

5.3.5 SLB's Role in Article 9 High-Yield Funds

When examining the role of SLBs in Article 9 bond funds, interviewees state that this instrument has facilitated the adoption of *high-yield* Article 9 funds. *High-yield* funds must maintain a minimum of 80% exposure to the *high-yield* credit rating segment (Wennerstein, 2024). The remaining AUM can be allocated to either investment-grade credit rating or liquidity (ibid). SHB, with current 90% exposure to *high-yield* bonds in their *high-yield* Article 9 fund, emphasises that many *use-of-proceeds* bonds have an investment grade credit rating, meaning that they have a credit rating of BBB- (according to S&P and Fitch) or above. In contrast, SLBs tend to be issued by smaller-sized firms with low credit ratings while still having KPIs linked to climate goals. This positions SLBs as a suitable choice for *high-yield* Article 9 funds, given that they need to invest in the *high-yield segment* while having sustainable investment as their primary objective to have the Article 9

classification. SHB emphasises that the large issuance of SLBs since 2021 contributes to the ability to start *high-yield* Article 9 funds and is furthermore a reason behind SHB's choice to start this type of fund:

"In the high-yield world, this is the opportunity for them to issue something that is linked to a climate goal" - Karin Göransson, Fund manager, SHB, 2024

"In the high-yield market, the supply is not as extensive, so we must also consider SLBs" - Klas Wennerstein, Fund Manager, SHB, 2024

"There is not as much use-of-proceeds in the high-yield world as there is in the investment grade world, and that is because the size of the companies is smaller" - Karin Göransson, Fund manager, SHB, 2024

"2021 was the prime time for SLBs, then they were issued like crazy, and that was when we also paid attention here. A lot of material came into high-yield, so that was also a reason for starting these [Article 9 high-yield funds]" - Klas Wennerstein, Fund Manager, SHB, 2024

"Certainly, it [SLBs] contributes to the ability to do it [Article 9 funds]; otherwise, there are many green bonds or use-of-proceeds bonds, but there is a risk of financing assets that already exist" - Klas Wennerstein, Fund Manager, SHB, 2024

Moreover, ODIN suggests incorporating KPIs related to sustainability goals into financing agreements can give investors more influence, especially with smaller companies. This is because larger companies with investment-grade credit ratings usually have no trouble securing financing, whereas smaller companies with low credit ratings may be more open to such arrangements. This suggests that SLBs are suitable for Article 9 *high-yield* funds seeking lower-quality bonds while supporting smaller companies in their transition journey and being able to incorporate sustainability:

"It also has a credit risk element, so all other things being equal, it should be more difficult for those companies to find financing. And if you can then come in and say: Yes, but we are comfortable with credit risks, but we want the company to set up these KPIs, then maybe you can have more influence and so on. And of course, these really large companies, they always find financing, so you have more to say with a smaller company, absolutely" - Nils Hast, Fund manager, ODIN, 2024

6. The Case

This section begins with an overview of Lannebo Fonder, covering its history, investment approach, and sustainability focus. It then outlines Lannebo's decision to introduce a new sustainable corporate bond fund in 2020 and make it an Article 8 (light green) fund despite the growing popularity of Article 9 (dark green) funds post-SFDR implementation in 2021.

By March 2021, asset management firm Lannebo Fonder, founded in Stockholm in 2000, had grown from a shared vision among two founders to a 60-person firm managing SEK 90 billion in assets. Throughout its history, Lannebo has worked towards its mission of seeking to generate the best risk-adjusted return through active ownership. Lannebo believed that its financial performance had validated its approach. From Lannebo's inception to March 2021, the firm started with an AUM of less than SEK 80 million, comparable with today's number of SEK 90 billion. *"Lannebo's most crucial success factor is, of course, delivering excellent results to our shareholders. Anyone who invested 10,000 SEK in Lannebo Small Companies 20 years ago has seen that amount grow to 150,000 SEK,"* stated Anders Lannebo on the occasion of Lannebo's 20th anniversary.

However, amidst emerging market trends, Lannebo's Board of Directors recognised the necessity for a shift in approach in 2020. With the emerging trend of sustainable debt, they felt Lannebo needed to jump on it. Over the years, Lannebo's investment approach has evolved in lockstep with advances in climate change and sustainability science. However, they were lagging in the fixed-income department. Therefore, Lannebo's fixed-income fund managers, Katarina Ponsbach Carlsson and Karin Haraldsson, were asked in 2020 to issue a New Fund Offer (NFO) for a sustainable corporate bond fund. However, in 2021, the new SFDR regulation came, and a problematic decision struck Lannebo: Were they labelling the fund as Article 9, subject to the most rigorous sustainability regulations, or choosing to classify it as an Article 8 fund with less stringent sustainability criteria? At the time, Lannebo decided to make it an Article 8 fund to be on the safe side, not risking an argument with the Swedish Financial Supervisory Authority. However, after the decision, the management team was struck by a statement and series of questions: *What are the trade-offs for Lannebo between an Article 8 and 9 corporate bond fund? How is it going to affect Lannebo's future?*

6.1 Lannebo Fonder - Independent Asset Management Firm Since 2000

6.1.1 Background to Lannebo Fonder

In the late 90s, Anders Lannebo and Göran Espelund found themselves at a crossroads within Swedbank Robur, sensing a growing constraint on their decision-making autonomy. Anders Lannebo was the CEO of Swedbank Robur, Swedbank's asset management subsidiary, from 1981 to 1999. In 1999, he transitioned to being the Chairman of the Board, and Göran Espelund took over as the CEO of Robur. Espelund and Lannebo felt that under Swedbank's ownership, the fund management company was increasingly driven by decisions in the bank's best interest over those of its clients. This led to a decision by Espelund and Lannebo – to break away from corporate constraints and embark on a new journey. After that, Espelund and Lannebo founded *Lannebo Fonder (Lannebo)* with a mission to create independent, actively managed funds that prioritise client interests, free from the constraints of a banking institution:

“They did so with the underlying belief that they truly believed in genuine active managed funds. Therefore, active management is something we have stood for throughout the years and is what we [Lannebo] are associated with. We dare to make active decisions. We dare to deviate from benchmark indices” - Emelie Wallin, Head of Third-Party Distribution, Lannebo, 2024

At this point, Esplund and Lannebo did not know that the IT crash was just around the corner. However, despite the headwinds of the IT crash, Lannebo demonstrated resilience and growth. Launching amidst the turbulence, Lannebo managed to increase its fund assets by a staggering 10,000% within five years, reaching an AUM of SEK 8 billion. A key catalyst for this robust trajectory was the introduction of the new Premium Pension System (PPM) in Sweden. This positioned Lannebo to leverage the opportunities the evolving financial landscape presented, contributing to its rapid growth. Esplund and Lannebo continued to develop and grow the independent asset management firm they founded. In recognition of the founders’ hard work, Lannebo was named Sweden’s premier active manager by Morningstar in 2018.

6.1.2 Investment Philosophy

Since Lannebo’s inception, three words have remained central to the organisation: transparency, clear communication, and cultivating long term relationships. These principles underpin Lannebo’s impressive track record, boasting an average annual return of 14% over three decades (Lannebo, 2021). Ever since the beginning in 2000, the company has had an investment philosophy with a steadfast commitment to active portfolio management and a bottom-up investment philosophy with a focus on fundamental analysis:

“Generally, I think we have slightly more concentrated portfolios than our competitors, which aligns with Lannebo’s overall philosophy focusing on fundamental analysis. We know our companies well, and in our daily work, we are as far from index-thinking as possible” - Katarina, Ponsbach Carlsson, Fund Manager Lannebo, 2024

Lannebo’s investment process to maintain active ownership includes five steps: screening, company analysis, dialogue, AGM², and nomination committees (see Appendix 8). They want lasting value when considering an investment rather than a contemporary gain. An example of this is that Lannebo is one of the asset management firms being engaged in most nomination committees in comparison to their competitors:

“In terms of our size, we are one of the fund management companies with representation in the highest number of nomination committees. Comparatively speaking, among other fund management companies in the Swedish market, this is also something we are strongly associated with regarding our active ownership. Through our involvement in nomination committee work, which also demands considerable time from the fund managers, it is not just about managing funds in front of the computer

² Annual General Meetings (AGMs)

screen. On the contrary, I would say. We are long term owners. So, I believe that this is how we become associated.” - Emelie Wallin, Head of Third-Party Distribution, Lannebo, 2024

Aligned with its investment philosophy, Lannebo aims to optimise returns while managing risks effectively, ensuring the best possible outcome for investors. Catering to institutional and retail investors, Lannebo’s integrated investment approach is built on tailored investment solutions aligned with their risk tolerance and financial objectives. Since Lannebo was founded in 2000, the company has managed to grow its product offering, which included a diverse range of actively managed mutual funds spanning Swedish and global equities and fixed-income securities. Among the fund offerings, the Small Cap fund stands out as Lannebo’s flagship fund, managing assets exceeding 23 billion SEK in 2022 (see Appendix 9).

6.1.3 Formalising a Sustainability Agenda

Lannebo’s sustainability engagement started in 2013 when they signed the UN’s Principles for Responsible Investment (PRI)(see Appendix 10). Their sustainability journey continued in 2014 and 2015 by implementing equality goals and establishing a sustainability council to drive these purposes forward in the future. In 2016, the management team of Lannebo started their sustainability training, and they began performing sustainability analysis of their funds. Lannebo launched their first sustainability-focused equity funds in 2018, *Norden Hållbar* and *Sverige Hållbar*.

In 2020, Lannebo published its first sustainability report, marking a significant step forward in its commitment to sustainability. Sustainability reporting became a pivotal aspect of Lannebo’s growth and value-creation strategy, underscoring its commitment to integrating sustainable principles into its operations. In addition, Lannebo laid out their exclusion criteria (see Appendix 11). Their criteria address a broad range of sectors, from tobacco and cannabis to controversial weapons and fossil fuels. This marks the initial step for Lannebo towards adopting more sustainable investment practices.

6.2 Launching a New Sustainable Fund

6.2.1 New Fund Offer (NFO) - Lannebo Sustainable Corporate Bond Fund

Recognising the evolving sustainable debt landscape, the fixed-income experts at Lannebo, Katarina Ponsbach Carlsson and Karin Haraldsson, were asked by the Board of Directors in 2020 to create a new sustainability-focused corporate bond fund. This fund was supposed to meet the increasing demands for sustainable funds among fixed-income investors according to Lannebo’s board members’ expectations. Doubtful about this new fund idea, Ponsbach Carlsson and Haraldsson ventured into uncharted territory to launch the *Lannebo Sustainable Corporate Bond* fund (*Sussie*),

with a management fee of 0.27-0.5%. Ponsbach Carlsson and Haraldsson were currently managing Lannebo's *Corporate Bond* fund and *High-Yield* fund; however, the new fund intended to have a sustainability-labelled fund name, requiring a minimum allocation of 50% of its capital to sustainable investments (Lannebo, 2024). Consequently, it would signal sustainability through its name without mandating 100% capital allocation to sustainable investments. The two fund managers conducted a mandate for the new *Sussie* fund, deciding to have a Nordic region focus (see Appendix 12). Furthermore, they decided to focus primarily on *use-of-proceeds* bonds, where the proceeds finance projects promoting environmental and climate sustainability or other socially beneficial initiatives, encompassing green, social, and sustainability bonds. Given Ponsbach Carlsson's and Haraldsson's scepticism about how investors would receive this new sustainability-focused fund, they decided to broaden the fund's mandate to be able to invest in *high-yield* bonds, aiming to deliver returns to investors while focusing on sustainability:

“Actually, the drive perhaps was not from us. It was more driven by the Board. Sustainable investments were very much in the spotlight [...]. This was necessary to have, so the Board wanted us to develop a proposal for a mandate for that type of fund. Then we sharpened it a bit and made it very broad so we could also invest quite a lot in high-yield” - Karin Haraldsson, Fund Manager Lannebo, 2024

6.2.2 COVID-19 Pandemic Drawback

Ponsbach Carlsson and Haraldsson launched *Sussie* on February 18th, 2020, before the COVID-19 pandemic started. There was positive sentiment in the credit market in the first few days. There were increasing inflows to corporate bond funds and rising prices on the bond market. However, toward the end of February, the market experienced a sudden shift, with concerns about the pandemic significantly impacting market sentiment. By then, money flowed out of the corporate bond fund market, resulting in significant price declines. Ponsbach Carlsson and Haraldsson characterised the market as experiencing a state of stress, exhibiting heightened levels of concern that bordered on irrationality. During the most volatile period, the primary market for new bonds closed completely (Lannebo, 2020). The Global downturn in the stock market and societal shutdowns were met by forceful stimulus packages from central banks and governments worldwide. Ponsbach Carlsson and Haraldsson identified it as a six-week complete crash of the market and a time when nobody wanted credit funds. Despite that, *Sussie* survived and performed relatively well compared to the market.

A few weeks later, the market started stabilising in April, with a focus on recovery. Later, during the autumn, the rumours of a vaccine started to spread, which calmed the market. During the autumn, the primary market for new bonds was open again. At this time, green bonds continued to grow in the market (Lannebo, 2020). A critical factor during this period was the persistence of low interest rates, implemented in the wake of the pandemic amidst a backdrop of stagnant global growth.

6.2.3 New Leadership

In 2021, during the ongoing COVID-19 pandemic, Lannebo faced challenges in identifying innovative investment opportunities, and with changing customer behaviour, a change in the organisation was needed. Hence, Lannebo's Board of Directors realised the importance of a fresh perspective at the helm. With extensive experience in the fund industry, from being the CEO of Nordea's Asset Management for six years and the CEO of Skandia Fonder for four years, Jessica Malmfors assumed the CEO role at Lannebo in August 2021. This transition marked a shift for Lannebo aimed at securing the company's continued relevance in the changing financial landscape. The recruitment of Malmfors was part of a broader generational transition at Lannebo, and later, in the same year, Johan Lannebo, son of the founder Anders Lannebo, assumed the role of chairman. Furthermore, co-founder Göran Espelund, the former active chairman and long-serving CEO, stepped back but remained on the Board.

Malmfors encountered several challenges upon assuming the CEO role at Lannebo in 2021. Her primary objective was to propel Lannebo's ongoing expansion. This involved penetrating a new demographic of savers, as several clients had been with Lannebo for an extended time. Malmfors underscored the necessity by positioning Lannebo as a frontrunner in sustainable investments to engage with younger audiences. Hence, Malmfors' initial focus as the novel CEO was to develop Lannebo's new ESG agenda. Founded on the principle that sustainable business practices are not only ethically responsible but also strategically advantageous. In other words, this approach was expected to yield the optimal risk-adjusted return and thereby attract new clients:

"Integrating the right sustainability aspects into the investment process is crucial for us to identify the winners of the future and, consequently, generate a good risk-adjusted return for our shareholders" - Jessica Malmfors, CEO Lannebo Fonder (Lannebo, 2023)

The idea was to construct an ESG strategy with Lannebo's fund managers doing the sustainability analysis of the portfolio companies, ensuring that all companies prioritise long term sustainable development. In addition, developing Lannebo's ESG agenda involved maintaining internal sustainability practices and actively championing ESG principles externally through collaborative initiatives with other asset managers and having regular conversations with the employees of the companies they invest in. The approach was built on regular discussions with the portfolio companies to learn about their respective sustainability efforts, culture, and long term goals. Malmfors believed this was the right approach to find ways to improve and be innovative, where the sustainability strategy was supposed to be based on not a one-size-fits-all solution but a customised approach that fits each company's unique needs and goals.

Malmfors played a vital role in Lannebo's increased dedication to sustainability. With Malmfors behind the wheel, the company had new energy and a new ESG agenda, aiming to attract

new fund clients through extra focus on sustainability. This was marking a new era for Lannebo, which was coming up with new leadership.

6.3 New Sustainability Regulation by the European Commission - SFDR

6.3.1 *The Decision to Make Sussie an Article 8 Fund*

Simultaneously with Malmfors' appointment at Lannebo, the European Commission introduced SFDR in 2021 (see description in Section 2.1). At this point, Lannebo had to label *Sussie* as an Article 8 or 9 fund. As mentioned, Malmfors' objective as the new CEO was to enhance Lannebo's position as a frontrunner in sustainable investments. The top management, therefore, initially pushed to label *Sussie* as an Article 9 fund. Furthermore, Sweden's domestic market share of Article 8 funds (in % of total assets) was 92%, making the distinctiveness of an Article 9 fund particularly conspicuous (see Appendix 6).

Ponsbach Carlsson and Haraldsson sat down to review the discussion with top management. They discussed whether they should label the fund an Article 8 fund, which entails promoting environmental or social attributes or make it an Article 9 fund, thereby having to prioritise sustainable investment as the primary objective. They acknowledged the multifaceted nature of launching an Article 9 fund. They had realised that while establishing an Article 9 fund presents opportunities to channel capital towards environmentally responsible initiatives and support businesses embracing sustainable practices, it also comes with certain drawbacks. For instance, they may face reputational damage if they invest in companies where sustainable practices are shown to be lacking:

"The biggest challenge is to keep track of sustainability risks and motivate why they are a sustainable company. It is still a reputational risk for us if something bad happens in a company that we have in this fund. [...]" - Katarina, Ponsbach Carlsson, Fund Manager Lannebo, 2024

Moreover, as *Sussie* was a Nordic-focused bond fund, the diversification possibilities were already constrained. In addition, the fund managers did not consider SLBs sustainable, adding another layer of complexity to fund diversification. Therefore, the fund managers solved this by having an unsustainable part in *Sussie*, where they include SLBs. Given this, deciding to label the fund as Article 9 would not allow to keep the unsustainable part of the fund, posing a challenge for the fund managers in terms of fund diversification:

"No, but you get an easier diversified portfolio if you also include SLBs. And that is where SLBs come in for us. They are essentially equivalent to our portion of the portfolio that is not sustainable - the brown part. So we have solved it by having such a portion in the portfolio to achieve sufficient diversification" - Katarina, Ponsbach Carlsson, Fund Manager Lannebo, 2024

Lannebo's management team also recognised a prevailing investor hesitancy to be the first movers in sustainable investing (Article 9). For example, several clients thought Article 9 funds were attractive but did not want to be first on the ball and take the risk. Furthermore, the administrative workload associated with an Article 9 fund is substantial, consuming significant time.

After careful consideration, Ponsbach Carlsson and Haraldsson deliberated and came to a decision: they would label the fund as an *Article 8 fund*. This would mean no significant changes for *Sussie's* fund investments. The Article 8 label would mean that Lannebo could keep the unsustainable part of the portfolio while still allocating 50% of AUM to sustainable investments to keep "sustainability" in the name. This approach, therefore, provided greater flexibility in adhering to regulatory requirements:

"We did discuss quite a bit back and forth about this with Article 9, or not [...]. Today, it is article 8 with at least a 50% share of sustainable investments. So, we have a clear goal for the proportion of the fund. [...] To be an Article 8, it is enough that you consider sustainability, and that is what we do at Lannebo. All our funds are Article 8 because we have exclusion criteria" - Katarina, Ponsbach Carlsson, Fund Manager Lannebo, 2024

6.3.2 *Sussie's Fund Flow and Performance*

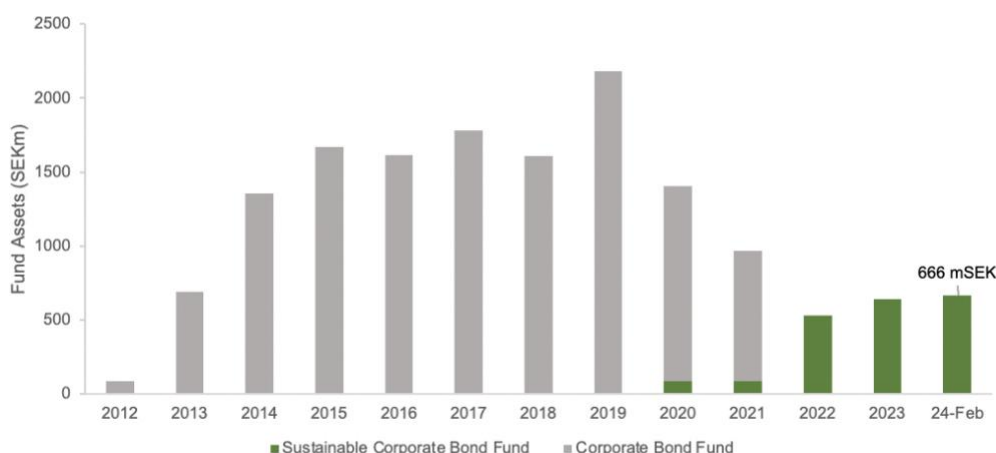
Lannebo had encountered challenging times with *Sussie* after the COVID-19 pandemic, characterised by significant outflows and limited inflows to *Sussie* (see Figure 6). Similar to *Sussie*, Lannebo's *Corporate Bond* fund, which did not focus on sustainability, also experienced challenges after 2019 with a high degree of fund outflows. Therefore, in 2022, approximately two years following the launch of *Sussie*, Ponsbach Carlsson and Haraldsson decided to merge *Sussie* with their *Lannebo Corporate Bond* fund. Since *Sussie* was categorised as an Article 8 fund, Lannebo did not have to divest many investments from its *Corporate Bond* fund following the merger to align with SFDR's Article 8 disclosures:

"To be completely honest, it is not like the money has poured into that fund [Sussie] even though we made it into a sustainable fund, which is largely why we also chose to merge the two funds" - Emelie Wallin, Head of Third-Party Distribution, Lannebo, 2024

On 24 February 2022, Russia invaded Ukraine. This war injected uncertainty into global markets, influencing investor sentiment, market dynamics, and risk perceptions. During this tumultuous period, Ponsbach Carlsson and Haraldsson faced new challenges with *Sussie*, which initially experienced negative returns (see Figure 7). The heightened risk aversion in the market led to a downturn in bond prices and a spike in credit spreads, impacting the fund's performance.

Figure 6

Fund Assets of Lannebo Sustainable Corporate Bond and Lannebo Corporate Bond (mSEK)



Source: Haraldsson & Carlsson (2023), Haraldsson & Carlsson (2024), Lannebo (2020), Lannebo (2021), Lannebo (2022)

Analysing historical data, Lannebo has surpassed its peers with a return of 8.9% compared to the peer average of 6.5% over the past year (see Table 5). All funds in the table are classified as Article 9 corporate bond funds, except for Lannebo's fund. Furthermore, *Sussie* has exhibited lower quarterly return volatility than Article 9 peers, which aligns with Appendix 5, showing that historically, Article 9 funds have been more volatile than Article 8+ funds. This stability in returns is consistent with Lannebo's investment philosophy, focusing on risk-adjusted returns. While the fund may not reach the highest performance peaks, it consistently avoids the lowest performance troughs, distinguishing itself from more volatile funds (see Figure 7).

Table 5

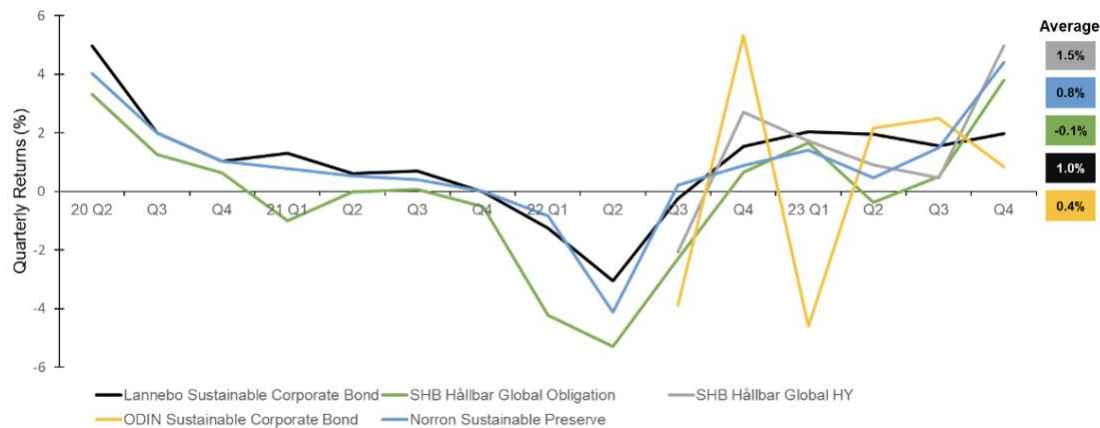
Peer Comparison of Fund Returns 2024-04-09

Fund	1 year	3 years, per year
Lannebo Sustainable Corporate Bond (<i>Sussie</i>)	8.9%	3.0%
SHB Hållbar Global Obligation	3.1%	-2.1%
SHB Hållbar Global HY	7.8%	-
ODIN Sustainable Corporate Bond	5.8%	-
Norron Sustainable Preserve	6.9%	1.7%
Average	6.5%	0.8%
Index*	5.8%	3.1%

* Solactive SEK IG Credit Index

Source: Morningstar

Figure 7
Peer Comparison of Quarterly Fund Returns 2020-2023



Source: Morningstar

6.4 Epilogue

As of the beginning of 2024, *Sussie* operates as a sustainable Article 8 fund and has 68% sustainable investments in Nordic companies, where 50-55% are *use-of-proceeds* (Ponsbach Carlsson, 2024) and the rest are bonds that Lannebo classify as sustainable according to their sustainability criteria. Moreover, Lannebo has a 22% exposure to the *real estate* sector, reflecting the fund's Nordic geographical scope (see Appendix 12). Given Lannebo's acknowledged need for fund diversification, the fund managers constructed an unsustainable part of the fund consisting of 44% *high-yield* bonds (see Table 6), whereas 10% are SLBs (Ponsbach Carlsson, 2024).

Table 6
Sussie's Credit Rating Distribution

	Credit rating	% of the fund
Investment grade	AAA	0.4
	AA+/AA/AA-	-0.1
	A+/A/A-	6.2
	BBB+/BBB/BBB-	41.8
High Yield	BB+/BB/BB-	41.9
	B+/B/B-	2.4
	CCC/CC/C	0
Default	D	0
Liquidity		7.4

Source: Lannebo Monthly Report, Feb 2024

Despite *Sussie's* attractive historical performance, Lannebo acknowledges that fund flows from the start have been below expectations, even from institutional investors. Furthermore, Haraldsson emphasises that fund investors are still predominantly fixated on fund returns rather

than the fund's dedication to sustainability. This dilemma adds an extra layer of complexity. It puts Lannebo in a situation regarding how the fund managers should position themselves to attract new fund investors to increase AUM:

“We have not had a huge inflow in that fund [Sussie]. We probably thought there would be even more from institutional investors” - Emelie Wallin, Head of Third-Party Distribution, Lannebo, 2024

While Lannebo decided *Sussie* would be an Article 8 fund, they demonstrated its commitment to Article 9 funds by launching its first Article 9 equity fund, the *Lannebo Europe Green Transition*, in 2022. Perhaps this indicates that they were unprepared in 2020 upon the launch of *Sussie*; nonetheless, they are now eagerly embracing the initiative and endeavouring to participate in SFDR's Article 9 fund landscape genuinely.

7. Discussion

The following section presents a discussion of the findings from the interviews. First, the initial research question will be answered, investigating Nordic fund managers' underlying motivations that drive them to initiate Article 9 corporate bond funds and other stakeholder views on the transition. Followed by a discussion regarding the rationale behind Lannebo's decision to rebrand their sustainable corporate bond fund to an Article 8 fund instead of an Article 9 fund to answer the third research question. Lastly, we answer the second research question by elaborating on the findings on SLBs' implications for Article 9 corporate bond funds. The answers to the three research questions will be discussed based on the literature presented in Section 3 and the findings from the analysis in Sections 5 and 6.

1. *What key drivers lead Nordic bond fund managers to issue Article 9 corporate bond funds?*
2. *What implications do SLBs have for the Article 9 corporate bond fund market?*
3. *What insights can be gained from Lannebo's Sustainable Corporate Bond fund, examining the trade-offs for fund managers between Article 8 and 9 corporate bond funds?*

7.1 Motivations for Article 9 and Article 8 Bond Funds

Previous research argues that fund managers are incentivised to take actions that boost total fund assets (Chevalier & Ellison, 1997). This is consistent with our findings for the first research question, suggesting increased investor demand for sustainable alternatives which has motivated fund managers to issue Article 9 bond funds. According to the survey results, fund managers rated client demand as, on average, a 4 on a scale of 5 driver in their decision to issue an Article 9 fund (see Table 4 and Appendix 7). This is consistent with Ferriani (2023) and Scherer & Hasaj (2023), showing evidence that Article 9 funds attract significantly more fund flows. Moreover, the results show that

fund managers find the Article 9 label to be a conversation starter with investors, making investors more accessible.

Furthermore, the findings show that institutional investors exhibit the highest interest in Article 9 corporate bond funds compared to retail investors. This can be explained by interviewed stakeholders, acknowledging that numerous institutional investors have pledged to achieve various emission reduction goals and participate in diverse sustainability initiatives. This phenomenon can potentially be understood through the findings of Riedl & Smeets (2017), which encompass the role of social signalling, which impacts investors' decisions to hold SRI. However, the institutional investor Forseke (2024) states that institutional investors are afraid of getting involved in scandals and, hence, are exposed to reputational risks and potentially greater business risks if they do not prioritise sustainable investments. These findings challenge the prevailing notion in recent academic literature that the demand for sustainable products stems primarily from ethical considerations (Riedl & Smeets, 2017). Instead, our study shows that institutional investors can be motivated to invest sustainably due to concerns about reputational risk and the possibility of facing increased business risks if they neglect sustainability considerations.

Furthermore, the findings show that the surge in client demand for Article 9 funds has led to a decreased emphasis on fund track records. This aligns with Bollen (2007), Benson & Humphrey (2008), and Renneboog et al. (2011), finding that traditional funds' net flows are more sensitive to past returns than SRI funds. Regarding fund returns, fund managers have not seen any superior returns in Article 9 corporate bond funds due to the smaller investment scope compared to Article 8 corporate bond funds. This can be explained by financial theory, which states that constraints placed on fund portfolios typically lead to diminished performance (e.g., Rudd, 1981; Hall, 1986; Diltz, 1995). In line with this, Hartzmark & Sussman (2019) find no evidence of outperformance by high-sustainability mutual funds. Therefore, our study suggests that despite the lower return potential of Article 9 bond funds, institutional investors also prioritise factors beyond profit maximisation, making these funds attractive to launch. This challenges the study by Dalmácio & Nossa (2004), suggesting that incentives for fund managers to increase AUM can give rise to *agency issues* between fund managers and fund investors, making fund managers prioritise strategies aimed at increasing AUM instead of dedicating time to active fund management aimed at maximising-returns. Instead, our findings show that fund investors care about other factors, such as social signalling and reputational risk, beyond sole profit maximisation.

SFDR aims to increase sustainable investment by providing transparency to investors (Swedish Financial Supervisory Authority, 2022). Consequently, fund managers argue that they face regulatory pressure from SFDR by having to label their funds with an Article classification. This increased transparency has driven fund managers (on average 3 on a scale of 5) to launch Article 9 bonds funds for reputational reasons. The prioritisation of the Article label for reputation, rather than solely focusing on the objectives of the Article 9 fund, is evidenced by the fact that the Article

9 funds in the sample do not demonstrate a higher average taxonomy alignment than that of Lannebo's Article 8 corporate bond fund (see Appendix 13). The taxonomy alignment is supposed to show how investments in a fund align with what the EU classifies as sustainable activities (see Section 2.1.2). Given that the Article 9 funds do not necessarily have higher taxonomy alignment than the Article 8 fund, this prompts questions about the effectiveness of SFDR within the fund setting. In line with this, Scheitza et al. (2022) findings suggest that the SFDR system is ambiguous and arbitrary, where many Article 9 funds do not meet the requirements.

In contrast, fund managers acknowledge that the risk of failing to fulfil the Article 9 requirements has resulted in fund managers downgrading funds from Article 9 to Article 8, thereby decreasing the number of Article 9 funds that do not meet the criteria. Hence, the small number of Article 9 bond funds in the market compared to Article 8 bond funds has facilitated differentiation opportunities for fund managers in the sustainability fund landscape. The findings from this study show that this is a critical factor for issuing Article 9 bond funds (see Table 4). The intention to differentiate in the fund landscape aligns with the findings of Bonelli et al. (2022), who concluded that unique funds can command higher fees. This could suggest that fund managers launching Article 9 funds have sought to carve out a distinctive niche in the market. However, we do not observe that certain managers overseeing Article 9 corporate bond funds impose higher management fees than Lannebo's Article 8 bond fund in this paper.

The supply of compliant bonds for Article 9 bond funds is not a driving factor in issuing or rebranding these funds, as there is a limited supply. Considering Article 9 corporate bond fund's niche nature and limited investment scope, more GSSS-bonds in the market are crucial for launching these funds. The limitation is also an explanation for Article 9 bonds still being a small part of the market (6% 2023). However, with the new CSRD initiative launching, which mandates that corporations provide credible sustainability information, and banks aiming to underwrite more GSSS-bonds, this will likely further expand the market for these bonds. Consequently, this might become a future driver for Article 9 funds.

Our study furthermore investigates the rationale behind issuing a bond fund as opposed to an equity fund. To our knowledge, this is the first study to explore this in the context of Article 9 funds. The findings show that fund managers prefer bond funds due to the possibility of creating a swifter and increased impact to lower risk. This is because the bond issuers' fear of not securing debt financing aligns their interests with the fund managers. Therefore, this possibly implies that there will be a continued increase within the sustainable bond fund market in the future due to their positive characteristics.

Additionally, this paper examines the trade-offs between Article 8 and Article 9 corporate bond funds through a case study of Lannebo Fonder. Hence, to answer the third research question, we have directed the discussion towards three primary areas: fund performance, fund flow, and

diversification. Starting with the performance of Lannebo's fund, *Sussie*, the fund has outperformed the index (see Table 5) and comparable Article 9 peers. This aligns with Lannebo's belief that investors prioritise returns, which resulted in Lannebo broadening the mandate to include *high-yield* bonds for greater returns. Moreover, Lannebo's performance compared to Article 9 peers can be explained from interviews, acknowledging that the limited investment scope negatively impacts returns for Article 9 funds, given that Article 9 must prioritise sustainable investment as the primary objective according to SFDR. Additionally, Appendix 5 shows that Article 9 funds' have experienced greater volatility in performance overall over the years 2020-2023. Hence, Lannebo's decision to classify *Sussie* as an Article 8 fund can benefit from a financial return perspective by constraining the fund as little as possible (Rudd, 1981; Hall, 1986; Diltz, 1995). However, even though *Sussie* has performed strongly financially, the fund managers empathise the low demand for the fund since its launch, and there has been a large amount of outflows since the merger with Lannebo's *Corporate Bond* fund (see Figure 6). Lannebo assumes the low investor demand for *Sussie* can be explained by investors seeking higher risk choosing *high-yield* funds instead of *Sussie*. In contrast, low-risk investors choose short term bond funds, leaving *Sussie* caught between two investment preferences:

"If they [fund investors] want low risk, they go for short term bond funds. But if they are looking for a bit more risk, they do not care about Sussi; they go for high-yield funds because they yield more" -

Karin Haraldsson, Fund Manager Lannebo, 2024

Another reflection of the low investor demand may be their limited dedication to sustainability. Despite launching *Sussie* as a sustainable corporate bond fund in principle, they only committed to the bare minimum of investing 50% of the capital in sustainable investments to reach the threshold for naming the fund as "sustainable". Therefore, deciding not to label the fund as an Article 9 fund with 100% sustainable investments may have led to the outflows. This is consistent with the findings of Ferriani (2023) and Scherer & Hasaj (2023), suggesting that Article 9 funds experience higher net capital inflows than other mutual funds. Furthermore, data shows that Article 8 (no SI) fixed-income funds experienced *net outflows* of USD 16 billion between January 2022 and July 2023, contrasting with Article 9 fixed-income funds, which saw *net inflows* of USD 16 billion (see Appendix 4). This aligns with Cosma et al. (2023), who found that Article 9 funds performed better than Article 8 and Article 6 funds during crises, as this period was one of geopolitical instability. This implies that Lannebo could have experienced greater net inflows in *Sussie* if it were an Article 9 fund, which aligns with Article 9 fund managers who confirm high investor demand for Article 9 funds.

Lannebo's investment philosophy builds on active ownership, meaning that Lannebo is engaged in the companies in which they invest. This supports a narrower investment scope, mainly in the Nordic region. On the other hand, this contradicts the fund's emphasis on diversification as the green bond market in Sweden primarily consists of real estate issuers, posing challenges in

attaining a diversified fund. *Sussie* has a Nordic geographical mandate, and given the high concentration of green bonds in the real estate sector, this indicates difficulty in starting a diversified Article 9 fund. Moreover, Lannebo's scepticism to include SLBs complicates diversification efforts, as SLB issuers typically span a broader spectrum of sectors beyond real estate. Hence, Lannebo has a non-sustainable part of the fund to enhance fund diversification. However, the unsustainable part comprises 44% of *high-yield* bonds, whereas SLBs represent 10%. Since Lannebo does not observe any premium associated with SLBs, the low proportion of SLBs cannot be justified solely from a return perspective. Instead, Lannebo acknowledges the inherent risk of investing in SLBs, particularly when the issuer fails to meet the targets, which could pose reputational risk. This is consistent with a study by Chen & Lai (2010), showing that reputation is another factor that can affect fund flows.

"There has been some talk about maybe trading them [SLBs] at a premium given that they are more sustainable. But so far, we have not seen anything, neither premium nor discount. But then you can also flip it and say that it also entails a risk. Because what happens if a company does not meet its KPIs, for example? Well, maybe that is a bigger risk than having a regular black bond where you will not get any negative headlines" - Katarina Ponsbach Carlsson, Fund manager, Lannebo, 2024

The findings show that Article 8 and Article 9 classifications involve advantages and disadvantages, as summarised in Table 7, and the optimal choice may vary depending on a fund firm's capabilities and strategy. For Nordic-focused fund firms, such as Lannebo, which take a cautious stance towards SLBs while prioritising fund returns, an Article 8 corporate bond fund may be in favour. Instead, a firm with a broader geographical scope, possessing a positive view of SLBs and focusing on institutional investors, may favour an Article 9 bond fund.

Table 7

The Trade-Offs for Fund Managers Between Article 8 and Article 9 Corporate Bond Funds

	Advantages	Disadvantages
Article 9	(1) Larger institutional investor demand (2) Decreased emphasis on track record requirements (3) Differentiation	(1) Limited investment space and scope (2) Reputational risk (3) Volatile financial performance
Article 8	(1) Larger investment flexibility (2) Higher expected returns	(1) Less sustainability impact

Source: Information obtained from analysis conducted by the thesis authors

7.2 SLBs Interplay for Article 9 Funds

Liberadzki et al. (2021) study investors' preference for SLBs over other *use-of-proceeds*, emphasising the distinct factor of an enforceable and direct monetary incentive for issuers to achieve

sustainability objectives. This aligns with the fund managers' opinions regarding SLBs' impact, as several fund managers suggest that SLBs, with relevant KPIs, can have a greater impact than the *use-of-proceeds* format. While *use-of-proceeds* bonds allocate proceeds towards sustainable single projects, SLBs can influence a company's overall sustainability performance. Article 9 funds that incorporate these SLBs can, therefore, achieve a more significant sustainability impact.

When examining the role of SLBs in Article 9 bond funds, several states that this instrument has facilitated the adoption of *high-yield* Article 9 funds. This can, therefore, imply that *high-yield* Article 9 funds will increase if SLBs continue to take market share in the bond market. Nevertheless, Fund managers highlight several disadvantages of SLBs, primarily their lack of transparency. Consistent with previous studies, such as Natixis (2021), investors are concerned about the greenwashing risk of SLBs due to their lack of transparency. Additional literature by Vulturius et al. (2024) highlights the same issue when comparing green bonds with SLBs. It emphasises that investors have less control and insights over how the SLB proceeds are used. Moreover, the interviewees align with Barbalau & Zeni's (2021) findings that firms that choose SLBs may exploit the lack of transparency and manipulate the situation. While Berrada et al. (2022) suggest companies may issue SLBs to demonstrate their dedication to sustainability credibly, the interviewees contested this claim. The consensus among fund managers is that SLBs are often perceived as a form of greenwashing rather than a sincere demonstration of commitment to sustainability.

Regarding the design of SLBs, fund managers argue that there is a need for more precise and well-evaluated KPIs and SPTs to decrease greenwashing risks. Prior research recognises investor apprehension regarding greenwashing, as issuers of sustainable bonds can potentially establish attainable SPTs owing to ambiguous definitions in SLB Principles (Liberatore, 2021). In addition, penalties for not meeting the targets may not be severe enough, incentivising issuers to prioritise attainable SPTs and potentially benefit from SLB issuance without reaching the goals (Liberatore, 2021; Kölbel & Lambillon, 2022). This is consistent with the findings of our study, where fund managers agree that the penalty associated with failing to reach a target is relatively small. Fund managers are, therefore, hesitant to invest in SLBs when issuers lack sufficient incentives to achieve the targets. This hesitation stems from the assumption that bond issuers may issue SLBs for reasons other than ethical considerations, such as accessing cheaper financing or engaging in social signalling.

The greenwashing risks, combined with the difficulties in tracking SLB proceeds (typically used for general purposes, ICMA, 2023a), result in several fund managers not classifying SLBs as sustainable investments without extra evaluation and assessments. This demands high analysis effort from fund managers, potentially explaining why SLBs constitute only 5% of the overall sustainable debt market while green bonds represent almost 50% of all sustainable debt issued. However, SLLs represent more than 15% of the market; therefore, a discussion of the relative size of SLLs versus SLBs can be relevant. In terms of lending, green loans occupy a relatively small portion of the market, with SLLs commanding the lion's share. This signifies a difference from the dynamics observed in

the sustainable bond market. Therefore, given their shared linking methodology, the difference prompts interest regarding the factors influencing the prevalence of SLLs over SLBs. A difference between the two is the oversight mechanisms: financial institutions actively monitor adherence to sustainability criteria in SLLs, whereas SLBs lack comparable institutional oversight of their KPIs and SPTs. Therefore, this can be connected to why fund managers need supervisors and legislation over the SPOs to become more stringent in assessing SPTs and KPIs. Similar to the existing landscape with credit rating agencies like Moody's and S&P, to enhance credibility. Hence, improved institutional oversight and constraints could be a way to increase the market demand for SLBs.

8. Conclusion

8.1 Concluding Remarks

Sustainability discourse has significantly intensified within the mutual fund industry in recent years. Through a qualitative method with 15 interviewees, this thesis aims to explore the SFDR implications for the fixed-income fund market and examines the varied responses to sustainable instruments, particularly SLBs, among diverse stakeholders. For the primary research question, various key themes emerged regarding the factors influencing the decision to issue an Article 9 corporate bond fund instead of an Article 8 or 6. Firstly, our findings show that the increasing demand for sustainability is a key factor, particularly among institutional fund clients. This is because several institutional investors have committed to sustainability initiatives and are exposed to reputational and business risks unless they prioritise sustainable investments. Consequently, while fund managers acknowledge that Article 9 bond funds may not outperform their Article 8 counterparts, institutional investors prioritise factors other than profit maximisation. This reduces the emphasis on track records for Article 9 funds, explaining the attractiveness of launching Article 9 corporate bond funds. Secondly, our findings show that the SFDR labelling system (Articles 6, 8, 9) has resulted in fund differentiation opportunities for fund managers. Article 9 fund managers strive to distinguish themselves from the prevailing market dominance of Article 8 counterparts. Thirdly, fund managers argue that they face regulatory pressure from SFDR by having to label their funds with an Article classification. This increased transparency has driven fund managers to launch Article 9 bond funds for reputational reasons, aiming to find ways to attract investors to increase AUM. It is also worth noting that for Article 9 funds, several fund managers prefer bond funds over equity funds. The reason for this is the stability of bond funds, offering a safer way for fund managers to participate in sustainable initiatives while achieving swifter and increased impact.

For the second research question, we conclude that the biggest implications SLBs have had on the Article 9 bond fund market are on the *high-yield* side. SLBs are commonly issued by smaller firms with low credit ratings seeking to enhance their sustainability efforts. This aspect fills a gap that *use-of-proceeds* bonds cannot address, as *use-of-proceeds* typically have investment-grade credit

ratings. Therefore, we find that SLBs contribute to the ability to launch *high-yield* Article 9 corporate bond funds. Interviewees, moreover, suggest that SLBs with relevant KPIs can have a greater impact than the *use-of-proceeds* format. Therefore, Article 9 funds incorporating these SLBs can achieve greater sustainability impact. Nevertheless, SLBs present several drawbacks, such as challenges in tracking their proceeds attributable to insufficient transparency, elevated risk of greenwashing, and heightened analytical demands compared to *use-of-proceeds* instruments. Consequently, these drawbacks have limited SLB adoption and impacted the overall sustainable corporate bond market.

For the case study, Lannebo's decision underscores the complex interplay between sustainability objectives, performance considerations, and risk management strategies in the evolving landscape of sustainable investing. Lannebo has shown that Article 8 corporate bond funds can integrate sustainability and prioritise returns, leveraging less stringent sustainability disclosures than Article 9 funds. Moreover, the case shows fund managers' challenges with Nordic geographical mandates in launching Article 9 corporate bond funds, particularly without including SLBs for diversification. Lastly, the findings show that Lannebo has experienced low demand for its Article 8 bond fund since its launch. At the same time, Article 9 fund managers show a high demand for their funds in the same period. This concludes that fund managers aiming to start sustainable corporate bond funds today will likely increase investor attractiveness with an Article 9 label.

8.2 Limitations and Suggestions for Future Research

This study includes three main limitations that can be presented as future research opportunities. Firstly, the case study format can be seen as a limitation, as can the ability to make generalisations based on the case. As this case study only addresses one firm, one cannot make larger assumptions. Thus, a suggestion for future research would be to conduct similar case studies on other Nordic asset management firms and other European asset management firms to examine whether the factors for choosing an Article 8 versus 9 fund apply to other firms.

Another constraint is associated with the limited number of interviewees and the dataset. A recommendation for future research would be to expand the pool of fund managers interviewed and conduct quantitative analyses to evaluate the performance of various Article funds. Moreover, in our study, it proves challenging to segregate the findings of the Article 8 and 9 funds' performance from only the Article type to other occurrences and factors playing into the fund flows and performance. Therefore, we suggest a broader dataset for future research to investigate how fund classification affects capital flows in different economic environments. These insights could guide fund managers like Lannebo in optimising their fund offerings to attract capital inflows.

Finally, given the recent introduction of the SFDR and its incomplete implementation, it is early to draw definitive conclusions regarding its complete impact on the fund market. Moreover,

since the launch of the new regulation, there has been a volatile period with the war in Ukraine and other geopolitical circumstances. Hence, future studies should test whether the identified consequences of SFDR, such as increased transparency and ESG awareness, are also present during other periods. Elaborating on the aftermath of the SFDR would provide important insights for policymakers in measuring the broader effects of individual regulations' impact on capital markets. On the same note, future studies should explore whether portfolio companies subject to PAI reporting will benefit from adopting the CSRD (applicable from 2024).

9. References

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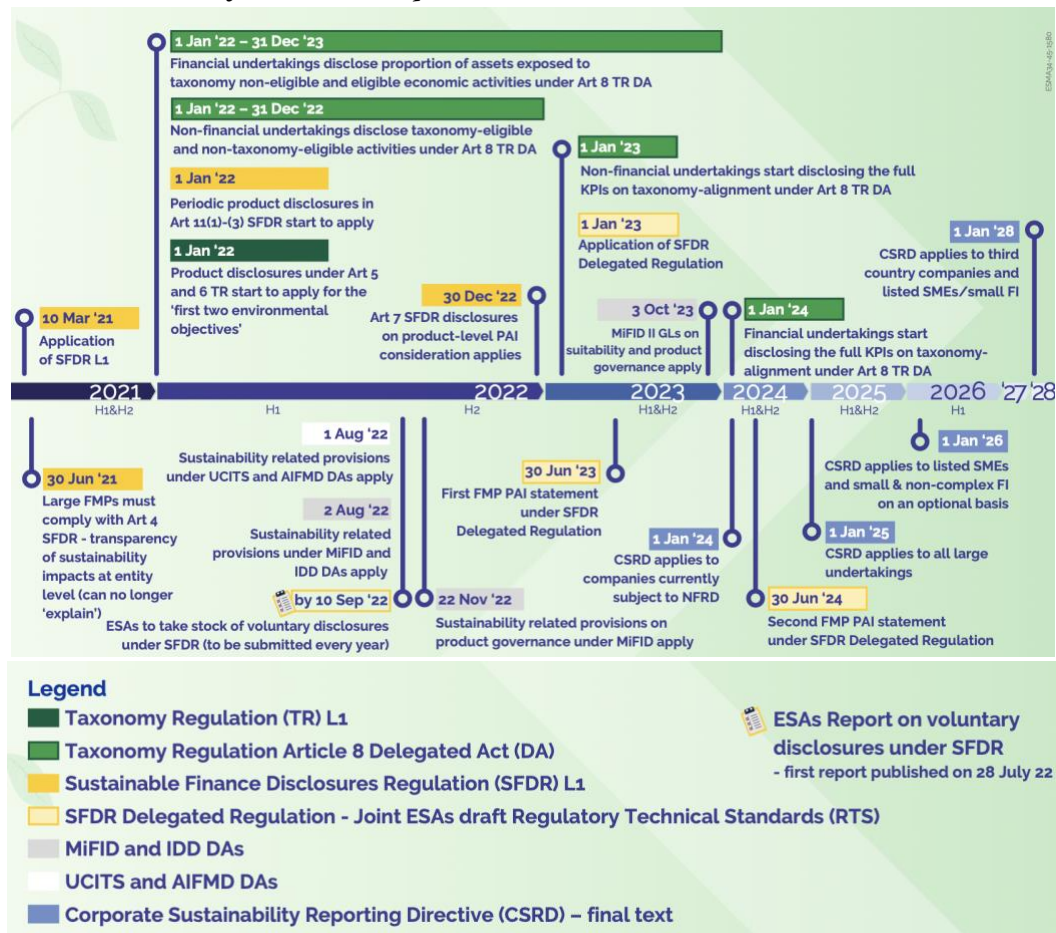
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10. Appendices

Appendix 1: Overview of Disclosure Requirements - EU Sustainable Finance



Source: European Securities and Markets Authority 2022, accessed March 2024

Appendix 2: Product Classification in SFDR

Level	Article	Description
Entity Level	Article 3	Publish on their website information about their policies on the integration of sustainability risks in their investment decision-making process.
	Article 4	Publish on their websites whether they consider or not the adverse impacts generated by sustainability factors and the due diligence policies adopted with respect to those impacts.
	Article 5	Publish information on how remuneration policies are consistent with the integration of sustainability risks on their websites.
Product Level Disclosures	Article 6	Provide in pre-contractual disclosures information on how sustainability risks are integrated into investment decisions and the impacts of sustainability risks on the returns of the financial products.
	Article 7	Provide in pre-contractual disclosures a clear and reasoned explanation of whether and, if so, how a financial product considers principal adverse impacts on sustainability factors.
	Article 8	Provide in pre-contractual disclosures and periodic reports information on how the financial product promotes and respects social or environmental characteristics and the methodology used for measuring social or environmental characteristics.
	Article 9	Provide in pre-contractual disclosures and periodic reports information on how the financial product contributes to the achievement of the sustainable objective and how the sustainable goal stands out from a traditional market objective

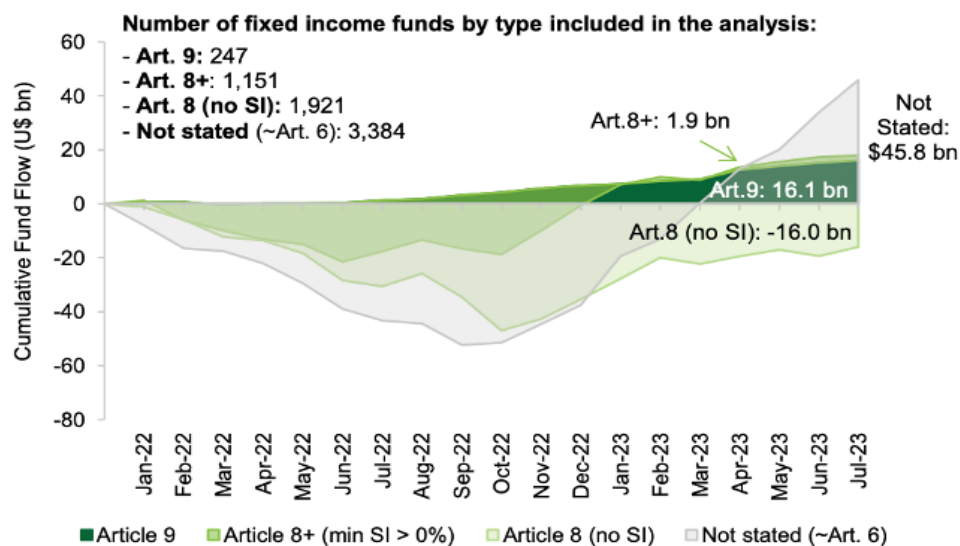
Source: EU Sustainable Finance Disclosure Regulation (SFDR) 2019/2088

Appendix 3: Summary of Relationship Between the EU Taxonomy, CSRD, and SFDR

	Purpose	Relationship	Role
EU Taxonomy	Serves as a classification system for sustainable economic activities. Applied within the frameworks of CSRD and SFDR.	Provides the foundational criteria for identifying sustainable activities required for reporting under CSRD and SFDR.	Facilitates alignment of investments with activities that are Taxonomy-aligned.
CSRD	Aimed at enhancing the quality and scope of corporate sustainability reporting.	Complements SFDR by supplying crucial data for SFDR reporting.	Mandates companies to report ESG metrics that are aligned with the EU Taxonomy. Incorporates these into SFDR reporting.
SFDR	Focuses on enhancing transparency in ESG disclosures and sustainable investment practices.	Utilises data from CSRD to enrich its own reporting and integrates it to provide a more comprehensive view.	Places emphasis on ESG disclosure to promote sustainable investment practices. SFDR reports integrating metrics from CSRD.

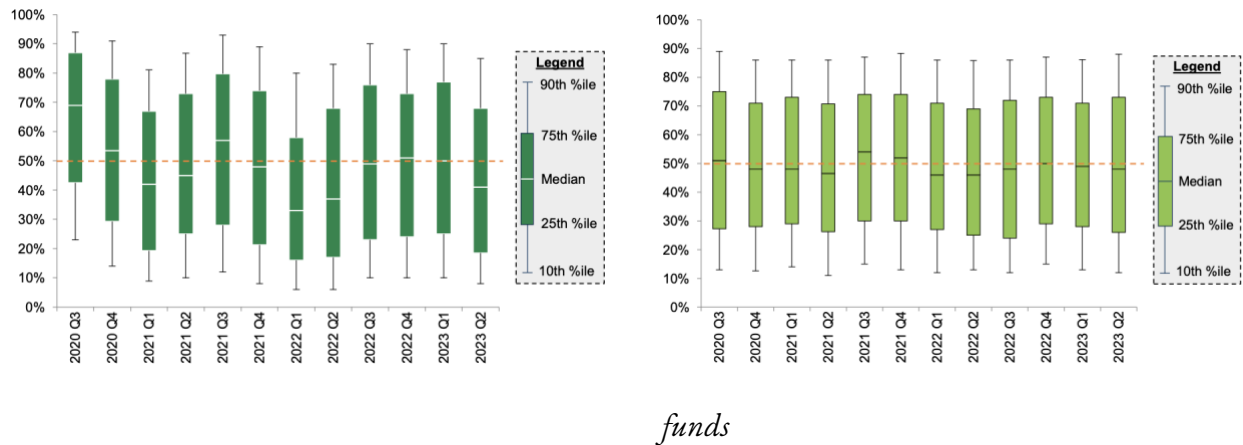
Source: Greenomy, 2023

Appendix 4: Cumulative fund flow of European Fixed Income funds by type (USD billion), Jan '22 - Jul '23



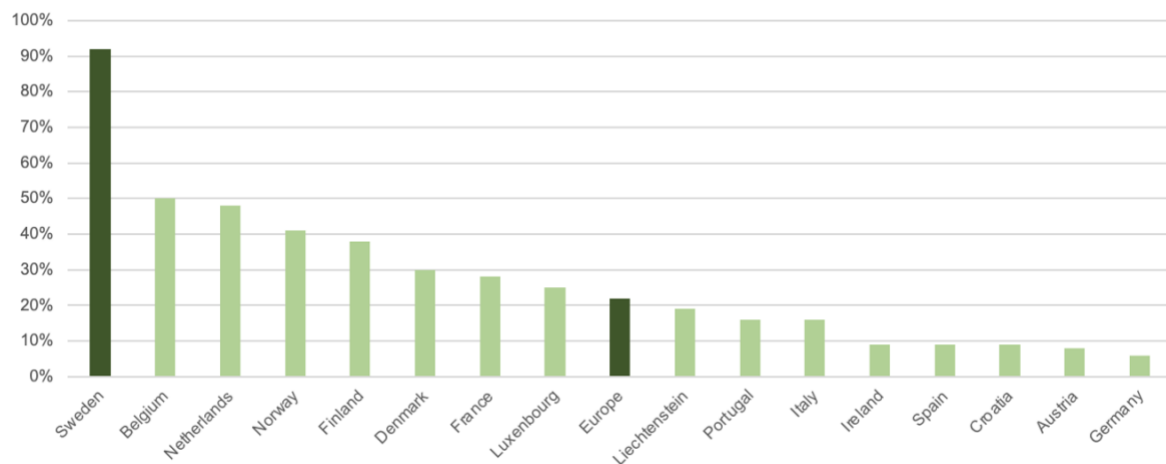
Source: Bioy et al. (2024)

Appendix 5: Distribution of Morningstar Return Percentiles: Article 9 funds and Article 8+



Source: Bioy et al. (2024)

Appendix 6: Domestic market share of Article 8 funds per domicile (in % of total assets 2021)



Source: Swedish Investment Fund Association. (2021)

Appendix 7: Answers from Survey by Fund Managers

	To what extent do you perceive regulatory pressure from the EU (EU Taxonomy and SFDR) as a driving factor for launching Article 9 funds? (1-5)	To what degree has the increased demand for sustainability from clients (retail and institutional) influenced the decision to launch Article 9 funds? (1-5)	How important are financial returns for Article 9 funds? (1-5)
Handelsbanken Hållbar Global Obligation	3	3	2
ODIN Sustainable Corporate Bond	4	5	3
Norron Sustainable Preserve	2	4	2
Handelsbanken Hållbar Global High Yield	3	4	1
Average	3	4	2

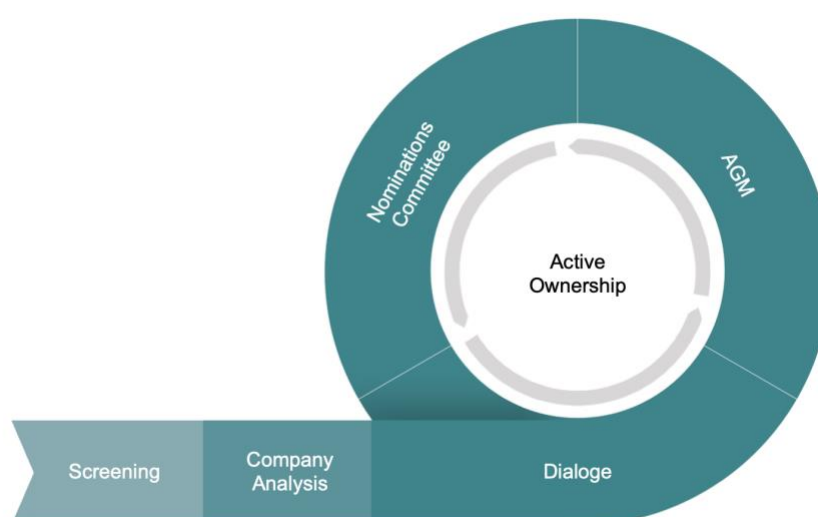
Question 1: (1) Negligible, (5) Strong

Question 2: (1) Negligible, (5) Strong

Question 3: (1) Very important, (5) Not important

Source: Interviews

Appendix 8: Lannebo's Investment Process



Source: Lannebo's Sustainability Report 2023

Appendix 9: Overview of Lannebo's Funds

Fund	Date Started	SFDR Classification	Sustainable Investments (2022-12)	Fund assets (k SEK) (2022-12)
Europa Småbolag – Eur	2016-10-17	Article 8	21%	1,348,560
Europe Green Transition – Sustainability Fund	2022-09-19	Article 9	95%	100,556
Fastighetsfond	2021-09-15	Article 8	12%	116,526
Fastighetsfond Select	2021-09-30	Article 8	11%	65,571
High Yield – Bond Fund	2015-01-30	Article 8	21%	487,729
Mixfond Offensiv	2013-05-16	Article 8	44%	2,044,140
Mixfond – Mixed Fund	2000-08-04	Article 8	38%	10,267,988
Norden Hållbar – Nordenfond	2018-06-14	Article 8	63%	161,813
Räntefond Kort	2001-11-12	Article 8	31%	5,136,328
Småbolag Select – Special fund	2000-10-31	Article 8	11%	2,077,443
Småbolag – Small Cap Fund	2000-08-04	Article 8	14%	23,637,748
Sustainable Corporate Bond	2020-02-18	Article 8	71%	531,114
Sverige Hållbar	2018-12-20	Article 8	64%	1,307,040
Sverige Plus – Sverigefond	2008-12-11	Article 8	57%	5,276,602
Sverige – Aktiefond	2000-08-04	Article 8	N/A	3,011,000
Teknik Småbolag – Globalfond	2019-11-07	Article 8	12%	6,461,096
Teknik – Ny teknikfond	2000-08-04	Article 8	9%	814,550
Microcap	2007-02-01	Article 8	57%	3,793,600
Nanocap	2016-05-31	Article 8	N/A	1,342,000
Oligio Global	2023-10-16	Article 8	N/A	N/A

Source: Lannebo Fonder, <https://www.lannebo.se/fonder/>, accessed March 2024

Appendix 10: UN PRI Principles for ESG Practice and Reporting

PRI Principles

Principle 1: *We will incorporate ESG issues into investment analysis and decision-making processes.*

Principle 2: *We will be active owners and incorporate ESG issues into our own ownership policies & practices.*

Principle 3: *We will seek appropriate disclosure on ESG issues by the entities in which we invest.*

Principle 4: *We will promote acceptance and implantation of the Principles within the investment industry.*

Principle 5: *We will work together to enhance our effectiveness in implementing the Principles.*

Principle 6: *We will each report on our activities and progress towards implementing the Principles.*

Source: “What is the PRI?” UN PRI, <https://www.unpri.org/about-us/about-the-pri>, accessed March 2024

Appendix 11: Lannebo Exclusion Criteria

Exclusion	Production (% of revenues)	Distribution (% of revenues)
Tobacco	0%	5%
Cannabis	5%	5%
Alcohol	5%	5%
Pornography	0%	5%
Gaming	5%	5%
Weapons	5%	5%
Controversial weapons	0%	0%
Fossil fuels	5%	5%

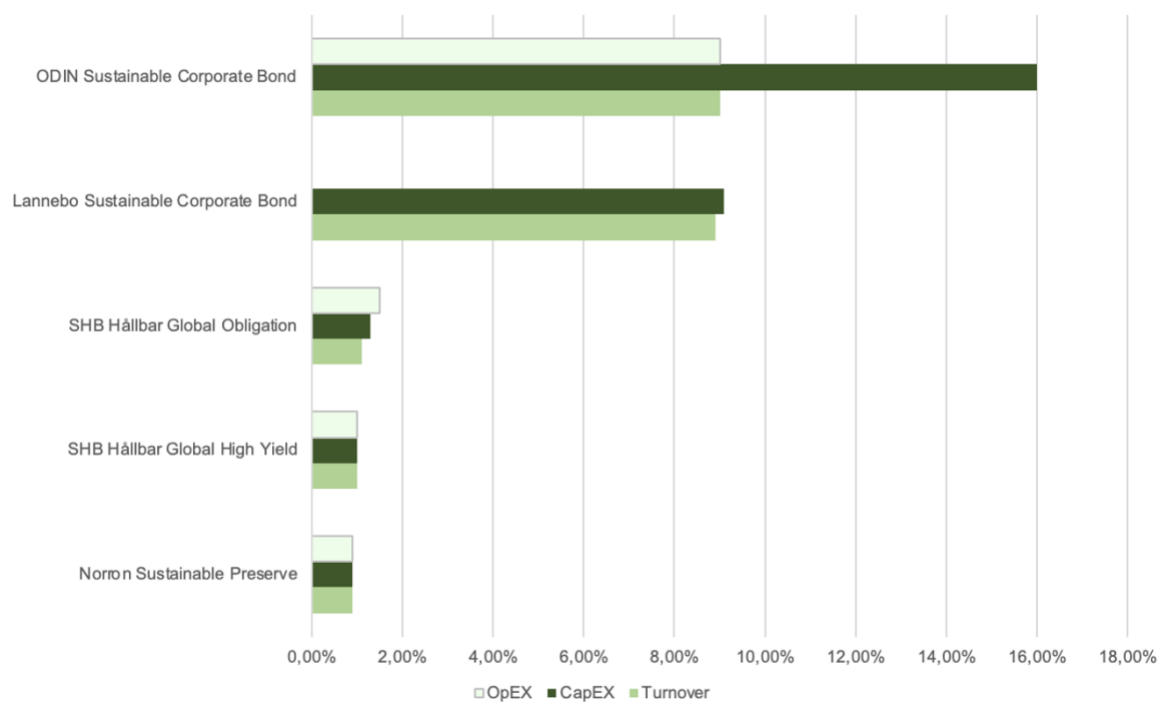
Source: Lannebo’s Sustainability Report 2020

Appendix 12: Lannebo Sustainable Corporate Bond, Portfolio Overview (%), as of Feb 2024

Top Ten Holdings		Sector Exposure		Regional Exposure
<i>DNB Bank</i>		<i>Real Estate</i>		<i>Sweden</i>
	3.6		22.4	47.7
<i>Castellum</i>		<i>Finance</i>		<i>Norway</i>
	3.4		20.0	25.3
<i>European Energy</i>		<i>Industrials & Services</i>		<i>Finland</i>
	3.3		14.7	9.9
<i>SEB</i>		<i>Energy</i>		<i>Denmark</i>
	3.3		7.9	7.8
<i>Storebrand Livsforsikring</i>		<i>Materials</i>		<i>Luxembourg</i>
	3.2		6.1	1.5
<i>Tryg Forsikring</i>		<i>Consumer Staples</i>		<i>Other</i>
	3.1		5.2	0.3
<i>Mowi</i>		<i>Consumer Discretionary</i>		
	2.9		5.1	
<i>Corem Property Group</i>		<i>Healthcare</i>		
	2.8		4.2	
<i>Terveystalo</i>		<i>Information Technology</i>		
	2.7		3.6	
<i>Fiskars</i>		<i>Communication Services</i>		
	2.6		2.7	
Total 30.9%		Total 100%		Total 100%

Source: Company documents (monthly report, Feb 2024)

Appendix 13: EU Taxonomy Alignment for All Interviewed Funds



Source: Fund Reports March 2024