

DEVELOPMENT OF INVESTMENTS IN THE SUSTAINABLE FINANCIAL PRODUCTS (CASE OF NORTH MACEDONIA)

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ABSTRACT

Sustainable finance and investing are broad concepts that have been started to be used recently and are an important component that will enable the shift of the countries towards more sustainable development. In particular, they intend to shift the finance towards projects and investments which intend to solve particular environmental and social issues. This research uncovered important information regarding the willingness of investors in North Macedonia to consider environmental/social factors in their investment decisions, and the readiness to invest in sustainable financial products in the future when they become available in the country. The results show that 87.5% of the investors care about the negative impacts that their investment might have on the environment or society. Moreover, they consider as important to take these factors into consideration, however, their main concerns with investing in sustainable products are the lack of global standardization of defining the green projects and unclear use of proceeds. Most investors, 95% have declared that they would be interested to invest in financial products which would pursue some environmental, and social goals, while at the same time achieving positive returns. Data shows that even though currently in North Macedonia there are not many options for sustainable financial products, there is a high level of interest from the side of the investors who want to contribute towards solving environmental and social issues through their investments.

KEYWORDS:

SUSTAINABLE FINANCE, SUSTAINABLE INVESTMENTS, DEVELOPMENT, ENVIRONMENT, SOCIAL FACTORS

JEL CLASSIFICATION CODES:

Q56, G 23, G11

1. INTRODUCTION

The development of sustainable financial products came as a result of a demand for investors to invest in new financial products which would take into consideration and/or address some environmental and social issues on the path of moving toward sustainable development. The European Commission defines sustainable finance as: “The process of taking environmental, social and governance (ESG) considerations into account when making investment decisions in the financial sector, leading to more long-term investments in sustainable economic activities and projects” (EC, 2022). This type of finance aims to shift finance towards a more productive use of capital and away from unsustainable practices which in the long term will result in value creation. Employing sustainable financing supports the flow of financial instruments and related services toward the development of projects with environmental and social impact. Sustainable development cannot occur on its own, and instead requires major global action from countries and global institutions which will support this movement by providing the necessary financing to enable sustainable economic development. These institutions have supported the creation of new financial instruments such as green bonds, sustainable bonds, environmental bonds, and green and sustainable loans, as well as new financial institutions such as green banks and green funds, in order to meet the growing demand.

Sustainable economy and sustainable economic development are also one of the strategic priorities of the Government of North Macedonia. Several measures and actions have been undertaken by the Macedonian Government to ensure sustainable economic growth, higher standard of living and quality of life, quality education, and environmental protection. Currently, in North Macedonia, there is a lack of sustainable financial products which are limited and exist only in the form of loans such as green loans to both household and corporate sectors and rarely social loans (for students, and retired individuals). Even though these products exist, they only take a small fraction of their loan portfolios. However, much more activities are planned for the future among which the development of guidelines for banks that will make it easier for their operation in the area of green financing, the introduction of green tax policies to discourage taxpayers from causing pollution, and the development of green bonds which will be issued to finance projects that enhance the energy efficiency, reduce or prevent water and air pollution, support sustainable agriculture and other environmentally friendly projects. The aim of these types of financial products is to make our economy effective, more competitive, and more developed.

2. LITERATURE REVIEW

Sustainable Finance is a broad term that includes finances, on one hand, and the allocation of these finances towards sustainable investments to address social and environmental problems on the other. Relatively recently the term ‘Sustainable finance’ started to be used for a market of finance that aims to create specific social and environmental impact at the same time while having a financial return. This type of finance has a very important role which is to shift finance towards a more productive use of capital which will result in long-term value creation. This shift is necessary because capital will be allocated to sustainable investments and activities, which in the longer term will foster sustainable economic, social and environmental development (HLEG, 2017).

Sustainable financing refers to financing all aspects of sustainable development, but sometimes it is used interchangeably with the related terms green finance and climate finance. While they are related to some degree, there are differences in the scope of the terms of what particular issues the proceeds address. While there are still discussions to make clear distinctions, some authors have tried to define the scope of each of these types of finances. In order to better follow and understand the scope of each of these terms it will be better to start and make a distinction from the term with the most-narrow scope which in this case is climate finance.

Climate finance is a subcategory of green/environmental finance, and it provides funds for addressing climate adaptation and climate mitigation (Spinaci, 2021). Mitigation finance covers the financial flows which are spent on projects and programs that help to reduce or eliminate greenhouse gas emissions, whereas adaption finance refers to investments made to increase the adaption of the affected parties to the negative effects of climate change. Climate finance has dual importance since large-scale investments are required to cut down emissions, but also financial resources are needed to adapt to the adverse effects and impact of climate change (UNFCCC, 2020). Green finance or environmental finance must be eco-friendly and contribute to poverty alleviation, covering the financing of improvement in areas such as environmental degradation, air and water pollution and scarcity, improper disposal of industrial medical and household waste, deforestation, and loss of biodiversity (Chowdhury, 2013). What distinguishes it from climate finance it is the fact that green finance has a wider scope and in addition to covering climate adaptation and mitigation, it also covers other environmental goals such as the ones mentioned above. Meaning that green finance seeks environmental protection by considering potential environmental impacts in investing and financing decisions. Sustainable finance, on the other hand, has an even wider scope as provides finances to address environmental, social, and governance issues.

- Environmental finance considers environmental issues when investment decisions are made and capital is allocated to address issues related to climate change mitigation, greenhouse gas emission, pollution prevention, waste management, water management, water quality, energy efficiency, use of renewable energies, and other similar issues.
- Social finance includes allocating finance to investments that address issues with which the society is faced such as human rights, worker’s rights, working conditions, inequality, health and safety, child exploitation, quality education, affordable housing, community relations, food security, access to basic services, etc.
- Governance finance aims to address issues related to management and employee relations, quality of management, accountability, business ethics, anti-corruption, reduction of the gender pay gap, the presence of

women and men in managerial positions, discrimination issues of employees based on gender, age, ethnicity, religion, and ability issues.

North Macedonia during the years has taken several measures to move towards a sustainable economy and sustainable economic development. For example, the National Bank of North Macedonia intends to implement activities that will contribute to the shift of a new 'sustainable' economy, with the intention of creating an ecologically clean and healthy environment to improve the quality of life of its citizens through introducing monetary instruments for promoting and stimulating green finances in the domestic economy. Moreover, it will offer the possibility of creating a 'Green Bonds' portfolio, raising awareness of the risks of climate change and taking action to contribute in the creation of a green and sustainable economy (NBRM, 2021).

Among other, the strategic priorities of the Government of the Republic of North Macedonia are also ensuring accelerated and sustainable economic growth, a higher standard of living and increasing the quality of life for its citizens, quality education available to all, and environmental protection, green development, and reduction of air pollution and the impact of climate change (Ministry of Finance, 2021). Ministry of Finance of North Macedonia plans to introduce new financial instruments in the domestic market in order to ensure more efficient development such as the so-called "development bond", "Green Bonds" and "Project Bonds". The development bonds are planned to be denar-denominated government bonds issued initially to individuals, with a possibility to be made available to the banks, pension funds, and other participants of the financial markets. The proceeds from this type of bond will be used to finance development projects in the country. Green bonds are planned to be introduced in order to support the transition towards a green economy. This new financial tool will finance environmental projects, with a particular focus on projects that enhance the energy efficiency, prevent or reduce pollution, implement integrated waste management systems, support sustainable agriculture, fishing, and forestry, protect the aquatic and terrestrial ecosystems, provide clean transportation and foster the development of environmentally friendly technology (MOF, 2021). These new instruments are envisaged to help and transform the economy to make it more competitive and will focus on the green transition. Project bonds are planned to be used as alternative funding to source financing of infrastructure-related projects, allowing investors to invest in, for example, energy sector-related projects (Ministry of Finance, n. d).

In the private sector in North Macedonia, sustainable financing currently takes the form of loans that commercial banks provide to households and companies. The following loans which are extended from the local banks can be considered sustainable loans and take the form of green eco credit for individuals/ businesses, auto loans, consumer loans for pensioners, loans for education, loans for women in business, and credit for mothers.

3. RESEARCH METHODOLOGY

This study was conducted in two parts. The first part conducts a literature review of existing literature and reports on sustainable finances in North Macedonia, while the second part of the study is based on analyzing primary data, which were collected through a questionnaire distributed to investors. The main purpose of the questionnaire is to provide evidence from Macedonian investors on the relationship between investment practices, sustainable financing, and sustainable investing. In this study, the design of the questionnaire was based on 21 closed-ended questions, with multiple-choice answer options, which is sufficient for the targeted research objectives. The questionnaires were distributed to Macedonian investors in an electronic format, using google forms. At all times, the identity of the surveyed individuals remained private, as no personal data (emails, names, and surnames) was required to be given or saved. Answers were obtained from 80 current investors and after that, the collected data were entered and processed by the IBM SPSS platform, while the figures were created in Excel.

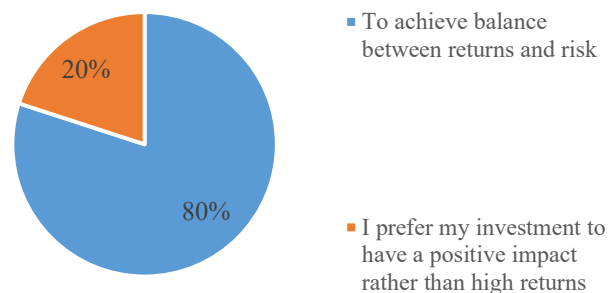
4. ANALYSES AND DISCUSSION OF THE RESULTS

The results of the questionnaire reveal important information for understanding the interest and readiness of investors in North Macedonia to take into account environmental and social factors when making investment decisions or investing in sustainable financial products.

The first question of the survey had the purpose to determine in what category the person's age falls into. In response to this question, most of those surveyed (40%) were between the ages 18-24, followed by 22.5% of the respondents between the ages of 31-40 and 12.5% between 41-50 years old. On the other side, we have fewer representatives of individuals of age between 25-30 years old (only 10 %) and 51-60 (10%), while individuals more than 60 years old, make up only 5% of the surveyed population. The participants in this survey are quite diverse age-wise, having representatives of all age groups, with the exception of individuals younger than 18 years old.

Out of the study population, 40 participants (50%) identified as female, and 40 (50%) identified as male. The collected information reflected that 42.5% of the respondents possess a master's degree or equivalent, and 37.5% a bachelor's diploma or equivalent, while 15% of the respondents hold a Ph.D., and only 5% of the surveyed population have a high school education. Investors when making investment decisions consider many factors. That is why the investors were asked a question on what is the most important factor that they take into account when making investment decisions, is it most important for them to only have high returns if they consider risk, do they care about the kind of project that their investment will finance or the kind of impact that their investment might have. The results are very interesting, as the majority of the investors 80% understandably want to achieve a balance between returns and risk, while the others, 20% prefer their investments to have a positive impact rather than high returns. This indicates that some of the investors would accept a return trade-off, meaning that they are ready to accept lower return rates if their investment will generate a positive impact on the society or environment. None of the investors have declared that they only want to gain high returns and do not care what type of projects their investment finances. These results are quite interesting as they indicate and confirm the many assumptions that high returns at all costs are not on top of the agenda for the investors, rather, they carefully assess the risks and want to achieve balance with the returns, and they are willing to accept social/environmental returns even if it means that they will gain a lower return on their investment.

Figure 1. When making the investment decisions, what is most important factor that you take into account?



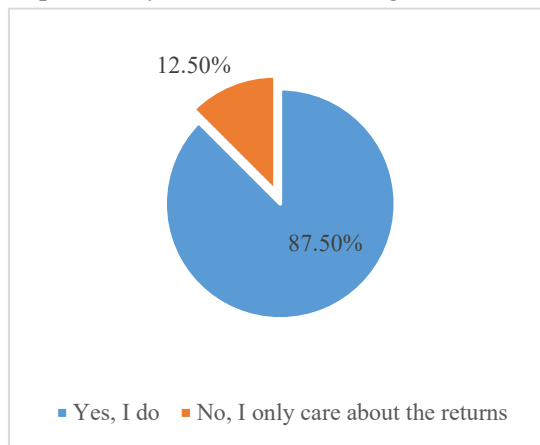
Source: Author's own research

The next question "When you are making your investment decisions, do you care about the potential negative social and environmental impact that your investments might have?" seeks to understand the respondent's perspective on whether they take into account the potential impacts of their investment choices and whether they make responsible investments by avoiding those that might have a harmful impact on society or the environment. According to the data acquired from the questionnaire (see Figure 2), only a very small percentage of people (12.5 percent) do not take into account the impact of their investment decisions because they are more concerned with profits. On the other hand, it is obvious from the answers that 87.5 percent of the respondents truly care and take into account the potentially harmful effects that their investments may have.

As the terms, sustainable financing and sustainable investing are fairly new, and these practices are not very well known in North Macedonia, it was very important to ask the respondents if they are familiar with these two terms, in order to be able to further continue with the questions. Out of the respondents, 15% have not even heard about the terms sustainable financing and sustainable investing, and 27.5% have heard of these terms but not fully understanding what the terms mean. While the majority of the respondents (57.5%) have declared that they have heard the terms and

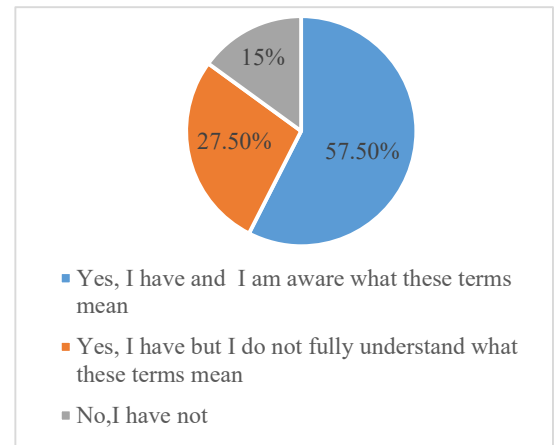
fully understand what these two terms mean (see Figure 3). From the obtained data it can be concluded that while most of the investors have heard these terms and most of them understand what these terms entail, there is still a very high percentage of investors or potential investors that have not heard or do not fully understand the meaning behind this type of investment, which might be due to the fact that in North Macedonia there are still not so many available sustainable financial products.

Figure 2. When you are making your investment decisions, do you care about the potential negative social and environmental impact that your investments might have?



Source: Author's own research

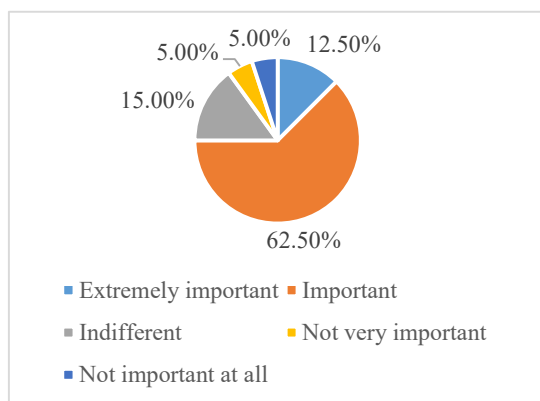
Figure 3. Have you heard about the terms sustainable financing and sustainable



Source Author's own research

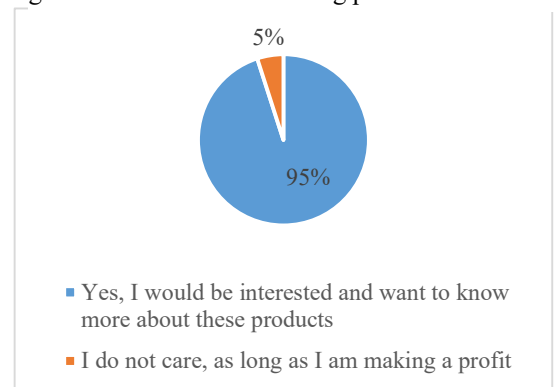
To better understand the investment strategies of the investors, they were asked how important the environmental and social factors in their investment strategies are. Almost two-thirds of the participants (62.5%), declared that in general, it is important for them to include environmental and social factors in their investment strategy, while 12.5% stated that they consider these factors extremely important to their investment strategy (see Figure 4). On the other hand, 15% of the participants stated their indifferent position towards this matter, incorporating these factors into their investment strategies, 5% think that these factors are not very important, while the remaining 5% consider these factors as not important at all for their investment strategy.

Figure 4. As a current investor, how important might be the environmental and social factors to your investment strategy?



Source: Author's own research

Figure 5. Would you as a potential investor, be interested to invest in financial products which would pursue some environmental, and social goal the same time achieving positive returns?



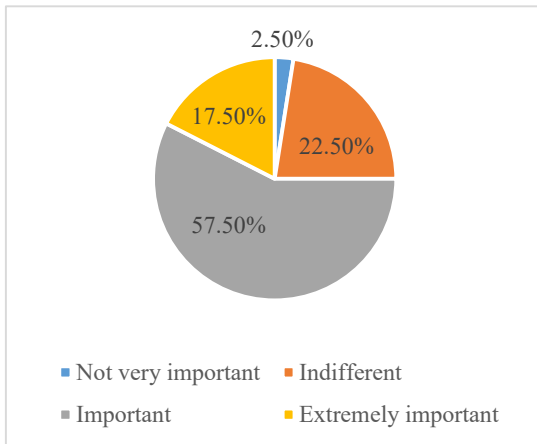
Source: Author's own research

The next question (Fig. 5) is intended to discover the investor's willingness to invest in sustainable financial products, which pursue either environmental or social goals when they become available in North Macedonia. The majority of the investors, 95% show positive interest, declaring that they would be interested to invest in this type of

product and want to know more about the products. The remaining five percent of the investors do not really care if the financial products in which they invest pursue some environmental or social goal, as long as they are making a profit. None of the investors, however, have answered that they would not be interested to invest in this type of financial product.

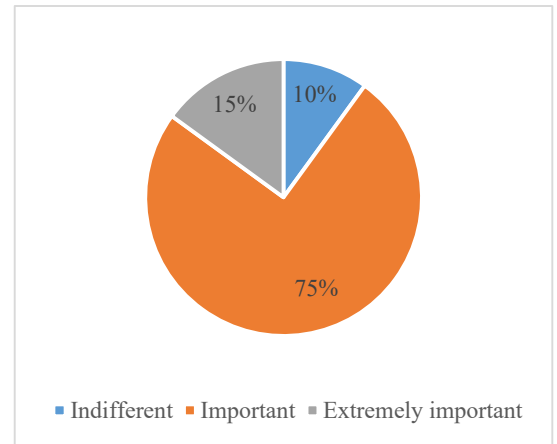
The following two questions aim to better understand the investor's view on making a positive impact on the environment and society, as they were asked how important is for them through their investments to make a positive impact on the environment and society.

Figure 6. How important is it for you, as an investor, that your investment has a positive impact on the environment?



Source: Author's own research

Figure 7. How important is it for you as an investor, that your investment has a positive impact on society?



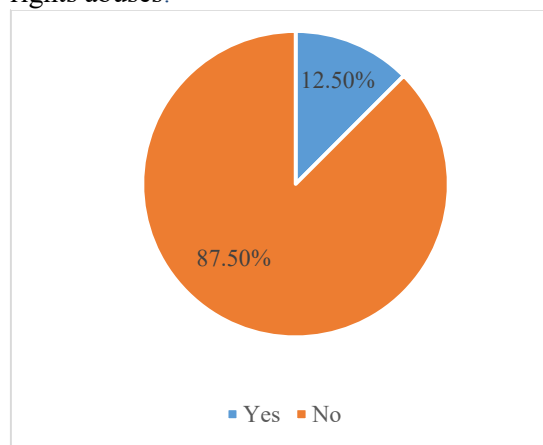
Source: Author's own research

For most of the investors, 57.5% making a positive impact on the environment through their investments it is important, while 17.5% of the investors have declared that for them the positive impact of their investment on the environment is extremely important. Some of the investors, 22.5% remain indifferent stand for this question, while 2.5% think that having a positive impact on the environment through their investment strategies is not very important. Out of the questionnaire participants, none answered that they think their investment having a positive impact on the environment is not important at all for them. When asked "How important is it for you, as an investor, that your investment has a positive impact on society", to further understand their stand on making a positive impact on society, 75% answered that for them it is important that their investment to have a positive impact on the society, while for 15% this matter is extremely important. The remaining 10% of the investors maintain an indifferent stand.

Next, the investors were asked three specific questions on whether they would invest in financial products issued by companies that had been accused or involved in activities resulting in some type of social or environmental abuses. First, they were asked if they would invest in products issued by companies that are complicit in human rights abuses, with the intention to see if investors when being aware that the company has been accused or is abusing human rights, would intentionally invest in those companies, and not let this factor affect their investment decisions. The majority of the respondents, 87.5%, have declared that they would not invest in financial products issued by companies that are complicit in human rights abuses, while for 12.5% of the respondents, this factor is not important and they have stated that they would invest in these companies (see Figure 8).

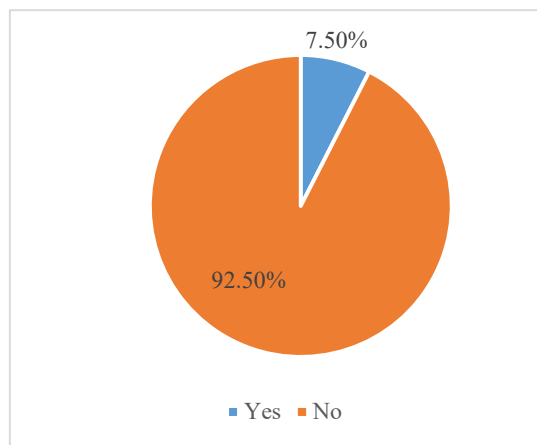
Investors were also asked if they would invest in companies that have been accused of child labor (Figure 9), in order to better estimate if investors care or do not care for child abuse, in this case, child labor being exploited by companies in which they would potentially invest. A high percentage of the investors, 92.5% would not invest in such companies, while for the remaining 7.5%, the company being accused of, or engaging in child labor is not an obstacle, and they would invest in these companies. From the gathered data, when compared with other similar questions, it can be seen that there is a lower percentage of investors who would still invest in companies if they had been accused of child labor.

Figure 8. Would you invest in bonds/stocks issued by companies that are complicit in human rights abuses?



Source: Author's own research

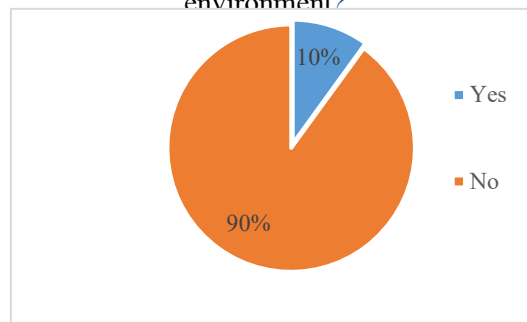
Figure 9. Would you invest in bonds/stocks issued by companies which have been accused of child labor?



Source: Author's own research

Investors were also asked if they would invest in companies that for example pollute the air, pollute the water, destroy wildlife, not manage adequately its waste products and similar issues. Most of the investors according to the obtained data, 90% care about the environment and when they make investment decisions, i.e. they would not invest in companies that in any way, cause harm to the environment, while the rest of the investors, 10% would invest in companies, which harm the environment (see Figure 10). These data show that 90% of the investors would, in this case, use the negative approach to sustainable investing, by not being willing to invest and not make financing available to these companies.

Figure 4. Would you invest in bonds/stocks issued by companies which cause harm to the environment?



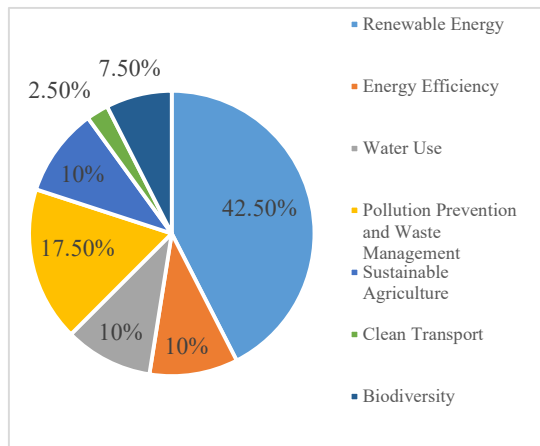
Source: Author's own research

There are a lot of environmental and social issues which the investors might address through their investments, which is why the questions in Figure 11 and 12 have the purpose to understand what particular issues they want to address in North Macedonia when sustainable investment products become available in the country. Several views were expressed since the respondents had the opportunity to choose one of the following options: renewable energy, energy efficiency, water use, pollution prevention and waste management, sustainable agriculture, clean transport, and biodiversity. These views surfaced mainly on what areas of the environment the investors perceived to be an issue and would invest in order to address that particular issue. Forty-two percent have answered that they would like to invest in renewable energy projects, and 17.5% want to invest in projects which would prevent pollution and better manage waste. Ten percent of the investors want to invest in projects which would improve energy efficiency, 10% would invest in project financing water use, and 10% would invest in projects for sustainable

agriculture. The remaining investors have declared that they would invest in projects for the preservation of biodiversity (7.5%) and 2.5% would invest in clean transport.

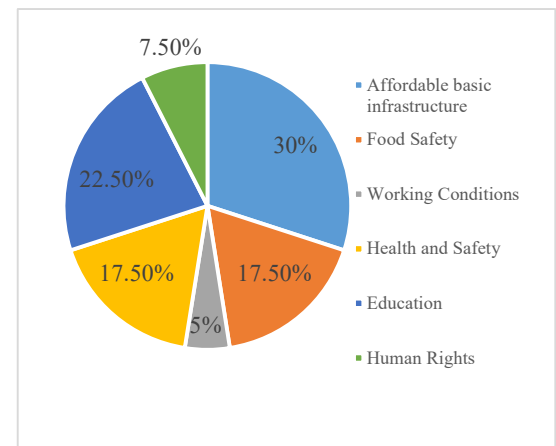
Affordable basic infrastructure such as drinking water, sewerage, sanitation, and transportation projects is the aim of 30% of the investors, indicating that North Macedonia still has a problem in meeting the basic infrastructure needs of its citizens, and this issue is one of the main ones which needs to be addressed and solved. Education is also a priority of investors since 22.5% have declared that they would invest in projects which would contribute to and solve the deficiencies in education, 17.5% of the respondents would invest in health and safety projects and 17.5% would invest in food safety projects. The remaining of investors have declared that they would invest in human rights projects (7.5%) and improving working conditions (5%). The results of these two questions turned out to be extremely important for this research, since the surveyed individuals had to choose, from a given list, the main environmental and social issues which they perceive to be the most important ones that require further investments to be solved.

Figure 6. Provided that you chose to invest in financial products which address environmental issues, in what particular projects would you like to invest?



Source: Author's own research

Figure 5: Provided that you chose to invest in financial products which address social issues, in what particular projects would you like to invest?



Source: Author's own research

In North Macedonia currently, there is a lack of sustainable financial products and they are limited to only loans issued by banks. Banks recently have started to include green loans in their portfolios, which are given to companies and individuals who want to invest in their homes or offices to be more energy efficient. Some banks also offer green loans to individuals who want to buy electric cars or hybrid cars, lowering carbon emissions. Banks also offer loans for students to pay for education, for women entrepreneurs or for retired individuals who otherwise have difficulties in obtaining a loan. However, other than loans, there are not so many other choices of sustainable financial products. The majority of the investors, 92.5% believe that in North Macedonia there should be more choices offering sustainable financial products, while the rest (7.5%) do not agree with this statement. The majority of investors, 77.5% declared that they would prefer to invest in a sustainable bond rather than a traditional one. However, as potential 'green investors', investing in green bonds in the future, they have some concerns. For most of the investors, 37.5% the main concern is the lack of global standardization of defining the 'green' projects and for 32.5% is the unclear use of proceeds. For the remaining 17.5% of investors, greenwashing is a concern and for 12.5% of the investors, the lack of reporting and transparency is a major concern for investing in green bonds.

Provided that there were more choices in North Macedonia and where they could choose to either invest in green or social bonds, 67.5% of the investors declared that they would invest in green bonds, while the remaining 32.5% in social bonds. Furthermore, investors believe that addressing environmental issues (80% of the investors) and social issues (87.5% of the investors), will lead to positive economic development.

5. CONCLUSION

This research revealed that investors in North Macedonia, show interest and desire through their investments to contribute and solve the environmental and social issues with which the society is faced today, in times when climate change has become a great threat. Investors show great interest specially to invest in financial products that finance renewable energy, pollution prevention, and waste management projects, as well as, affordable basic infrastructure (drinking water, sewerage, sanitation, and transportation), education, health, and safety projects. Even though currently in North Macedonia there is a lack of products financing such projects, there is a high demand and immense potential for development of such investments, since 77.5% of the investors have declared that they would like to invest in a sustainable bond rather than a traditional one.

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