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ESG, Green Growth & Employee Capitalism: G7 Roadmap for the Fifth Industrial Revolution

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The present primer is the third of a series of seven essays¹ summarizing some of the comments made by leading experts attending the **Singapore Economic Forum EU ASEAN Roundtable** held 12 November 2020 and the **WPC & G7 Pensions Global Financial Forum (GFF)** held 14 – 16 December 2020, titled *Innovation, ESG & Inclusive Growth Transforming Capital Markets*. All thought leaders and asset owners cited here spoke at the latter event, in their personal capacity, except otherwise indicated.

The authors of this article, who co-chaired the **Biarritz Summit/G7 Pensions Forum**², held in **France's** Northern Basque Country, 26 August 2019, took stock of the recent rise in demand for ESG-orientated and impact-driven investments across asset classes, including fixed income: greenium, the fact that most green bonds now trade with a lower yield than comparable conventional bonds, is a natural reflection of changing risk/return perceptions, notably from the part of employee-nominated pension board members (trustees) who represent broad cross-sections of society at large. Call it fiduciary capitalism in action!

“Greenium means most green bonds now trade with a lower yield than comparable conventional bonds, a natural reflection of changing risk/return perceptions, notably from the part of employee-nominated pension board members in G7 nations, who represent broad cross-sections of society at large: call it fiduciary capitalism in action!”

We talked to **Bertrand de Mazières**, DG Finance, **European Investment Bank (EIB)**, the **Luxembourg**-based European Union (EU) development finance institution and the world's leading supranational issuer of fixed income instruments. Mr. de Mazières delivered the keynote address titled '**Green Bonds, Social Bonds, Real Assets & Financial Innovation: What We've Learned So Far**', the opening speech of the session on 'ESG Revolution: The Centrality of **Climate Finance**, Social & Societal Engagement in the Post-Covid Era.' The ESG finance pioneer insisted on the dual role played by sustainability-driven fixed income investments: not only do they fund additional [social, energy and transportation] infrastructure projects, but they also induce issuers, institutional investors, and governments alike to adopt stronger stances re the mounting environmental and social emergencies of our time, made all the more acute by the **Covid-19 pandemic**.

David Zahn, Head of Sustainable Fixed Income, **Franklin Templeton**, addressed ESG in bond markets, focusing on the United Kingdom and the **European Union**. He thought that variations by country always have some (degree of) relevance. So, too, have considerations relating to the drivers of expected excess return (or 'alpha' themes) as an investment criterion. These two taken together, geography ("countries and governments") and alpha dynamics, help to form a picture. Zahn took questions from some of the pension experts and board members in the audience:

- “You are one of the pioneers in assessing and applying ESG in/to fixed income markets, here in Europe. Is it possible to put together the various factors [some more difficult to quantify] to form a coherent model?”

Zahn thought so, giving practical examples drawn from his interaction with fixed income issuers, both public (sovereign debt) and private (credit).

- Changes in weighting of ESG factors seem to be the subject of changing socio-economic perceptions etc. Of the E, S and G strands, there appears to be increased emphasis on the E, environmental, factors: climate change related in particular.
- At the moment, in many **European markets**, interest in G, governance, factors appears to centre round labour relations and corporate governance issues e.g. levels of top management pay; ratio of top management pay to average employee pay.
- “How do you **add alpha in an ESG/bonds context?**” “We’re not going just for best in class... Where you can really add value in the fixed income space is by selecting interesting companies that may be rated as mediocre at the moment [maybe BB], but management has identified the issues and started on the journey [to fix them]
- On an issuer level, engagement is essential, including thematically: for every company, we look at **water usage** and **pollution**, and **CO2 emissions** [and track progress and areas which need improvement]
- How might a potentially unbalanced **EU–UK Trade** and Cooperation Agreement³ (TCA) affect the UK situation? David Zahn thought that the UK jobs market would probably do well in the short-medium term whatever the outcome. Some of the board members and pension experts in the audience expressed a degree of optimism re **Britain**, discounting the risks of pressure on the **£ sterling** in foreign exchanges markets.



Understanding EESG, Greenium and the Innovation Imperative

pictured here clockwise:

Bertrand de Mazières, DG Finance, European Investment Bank (EIB)

Gina M. Raimondo, US Commerce Sec., founder, Point Judith Capital

David Zahn, Head of Sustainable Fixed Income, Franklin Templeton

Dr. Olivier Mousson, President, Société pour l’Encouragement de l’Industrie Nationale, Europe’s oldest economic research center and think tank

David Weeks and Nicolas Firzli also sat with **David H. Webber**, Boston University School of Law, author of the critically acclaimed book, “Rise of the Working-Class Shareholder: Labor’s Last Best Weapon”, to gauge the potential policy contours of the **Biden White House** when it comes to Employee, Environmental, Social and Governance (EESG) interests at this critical juncture for the future of America and the world economy.

“ESG-focused investors—I use former **Delaware Supreme Court** Justice Leo E. Strine Jr.’s term EESG to emphasize employees—the U.S. legal and regulatory perspective has truly moved from darkness to light in a matter of months. Last summer, new regulations adopted by the Trump Department of Labor (DOL) directly threatened fund fiduciaries that incorporated EESG factors in investing and tried to shift the presumption against shareholder voting by pension funds”. The **Boston University** scholar explained that the Trump DOL walked back some of the harsher aspects of the new rules. Had these actually been implemented, they could have set back U.S. EESG investing by decades, silencing shareholder voice, and further opening the gulf between the U.S. and the rest of the world on these issues. “The outcome of the presidential election changed this quite directly”.

“For EESG-driven investors, the U.S. legal and regulatory perspective has truly moved from darkness to light in a matter of months! Last summer, new regulations adopted by the Trump White House threatened fund fiduciaries that incorporated EESG factors and tried to shift the presumption against shareholder voting by pension investors. The outcome of the presidential election changed this quite directly [...] If the Biden Administration acts this year, it can shape sustainable finance for years to come”

The authors remarked that Marty J. Walsh, the incoming **US Labor Secretary**, is the former mayor of **Boston**, a former union leader,⁴ perceived as culturally aligned with the centrist tenets of Rerum Novarum,⁵ also known as ‘**Rights and Duties of Capital and Labor.**’ Dr. David Webber noted that “the prospects for new legislation revising the Employee Retirement Income Security Act, **ERISA**, to accommodate EESG investing have never been better, and the Walsh DOL seems eager to do the same on the regulatory level.”

Clearly, instead of facing a hostile administration, socially conscious investors will now be greeted by the most supportive American administration yet: “now is the time for EESG investors to push The White House and Capitol Hill to take action. One mistake that prior administrations have made, both Republican and Democrat alike, is to wait until the end of their terms to act on these issues. The Bush Administration acted in 2008, the Obama Administration in 2015, and Trump in 2020. If the **Biden Administration** acts this year, it can shape the EESG space for many years to come, regardless of the outcome of the 2024 presidential election.” More recently, Secretary Walsh also signed a petition calling for universities to create **LGBTQ+** (lesbian, gay, bisexual, and transgender+) resource centers on campus and include gender identity in non-discrimination policy, yet another sign that things could be changing for the better in America and the world – here, too, the “Biden effect” may represent “a turning point” with lasting impact across key **financial markets** and jurisdictions, including Britain and the European Union.⁶



Gender Equality and Employee Capitalism: The Time is Now

pictured here clockwise:

Renaye Manley, Dep.Dir., Service Employees Intl. Union (SEIU),
fmr. Member, Advisory Board, Federal Reserve Bank of Chicago

Prof. David H. Webber, Boston University School of Law (BUSL)

Daniel Pedrotty, Director, North America's Building Trades Unions

Deborah Goldberg, Treasurer & Receiver General, Massachusetts
Chair, Mass. Pension Reserves Investment Management (PRIM),
the state's \$ 90 bn. public employees and teachers' pension fund

On 12 March 2021, Dr. Webber also chaired the Roundtable on **The Framework for Inclusive Capitalism**⁷, a new compact between business, government and American workers. The roundtable brought together some of the leading progressive voices in North America, including (pictured here), Renaye Manley, Dep.Dir., Service **Employees Intl. Union**, SEIU, fmr. Member of the Advisory Board, **Federal Reserve Bank of Chicago**, Daniel Pedrotty, Director of Capital Strategy, North America's Building **Trades Unions** (NABTU), fmr. Director, Office of Investment, **AFL-CIO** and Deborah Goldberg, Treasurer & Receiver General, Massachusetts, Chair, **Mass. Pension Reserves Investment** Management (PRIM), the state's \$ 90 bn. public employees and teachers' pension fund.

David Webber observed that “too much of the game of economic growth has gone to a tiny sliver of society while worker economic welfare has declined.” Unrelenting attacks on trade unions and labor organizations and the systematic suppression of employees’ voice means the “game is often rigged against workers [...] dashing the American dream for millions [of our compatriots] and threatening democracy itself”. It was agreed that “we have to promote diversity, equity and inclusion [...] What can **institutional investors**, including asset owners do to restore the balance”? The authors of this article believe that the answer lies within pension funds and their boards: we call it fiduciary capitalism.

The notion of a Fourth Industrial Revolution was first advanced in the United States by contrarian economists like Robert J. Gordon in their work on the ‘new economy’ and the ‘internet of things’,⁸ which, in turn, owed a lot to earlier research by **Canada**’s H. Marshall McLuhan re the electric-information age.⁹ It was then popularized in the second decade of the century by business leaders and policy thinkers, notably in **Germany** (Kagermann and Wahlster spoke of ‘Industrie 4.0’ as early as 2011) and **Switzerland** (Davos, 2015) etc.

We sat with **Olivier Mousson**, President, Société pour l'Encouragement de l'**Industrie Nationale** (SEIN), Europe's oldest economic think tank, to discuss how this important concept would play out, as it were, against the background of the Post Covid World Economy. Dr. Mousson argues that institutional investors need to be actively engaged in **France**, at national level, as well as in the EU. Going forward, they'll have to be "more conscious than ever of the pressing need for an ambitious industrial strategy", rooted in "local production cycles with more resilient supply chains", in essence, "building the agile and mobile industry of the future." N. Firzli observed that the notion of reindustrialization was now "moving center stage in the **United States**, Britain and **Australia**: a powerful investment trend that can only gain more momentum in the coming quarters" [...] insisting that, beyond the lingering Covid Crisis, "reindustrialization will also benefit from the United Nations Sustainable Development Goals (SDG-Driven Finance), intensifying Sino-American competition (Age of Geoeconomics) and the employee-led fiduciary awakening (Employee Capitalism): it will be one of the essential features of the **Fifth Industrial Revolution**."

In an interview with Bloomberg (1 April 2021), **U.S. Commerce Secretary Gina Raimondo**, a venture capital and private equity veteran, and keen proponent of the notion of industrial renaissance, "whereby law, diplomacy and economic growth are considered on a unified geoeconomic plane"¹⁰, summed up the nascent **Biden Doctrine**: "we've seen a decline of our production of [advanced] semiconductors and that, of course, makes us vulnerable" [...] "We need to rebuild our manufacturing operations here [at home], increase **research and development** [bringing together government, corporations and institutional asset owners] so we can stay at the leading edge of these critical technologies." Ms. Raimondo's bold approach to trade and economic strategy echoes the prevailing view amongst **China's** policy thinkers: more developmentalist than neoliberal, thus, perhaps, marking the end of four decades of *laissez-faire* in Washington D.C. (1980 – 2020).

D. Weeks, N. Firzli and the Hon. Nick Sherry observed that PM Boris Johnson has put these issues at the forefront of the **47th G7, Carbis Bay Summit**, to be held 11–13 June 2021, thus helping the world "fight, and then build back better from coronavirus and create a greener, more prosperous future."¹¹ N. Sherry explained why "the presence of **Australia**, India and South Korea as keynote guest countries to this year's G7 constitutes a significant strategic decision", acknowledging the need to strengthen financial ties to EurAsia-Pacific nations whose economies now constitute the engines of global growth, alongside China and the United States . . .

The upcoming **G7 Pensions** dialogue, held in London and via video-link **11 June 2021**, on the sidelines of the **47th G7**, will include a special session on 'LT Investment, Climate Finance & The Firm of the Future' co-chaired by the Hon. Nicholas Sherry, Suzanne Bishopric, M. Nicolas Firzli and David Weeks, with leading UK, EU, US, PRC, AUS., CAN. and **ASEAN** pension executives, corporate leaders and policy thinkers.¹²

ENDNOTES

- ¹ Firzli, M. Nicolas J., and David Weeks. "Asset Allocation & Risk Management in a Fractured World Economy." *Institutional Investment Research (IIR)* (2021) https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3793199
- ² Firzli, M. N. J. (2020). CR/Réunion du G7 des Fonds de Pension d’Août 2019 : Les Objectifs de Développement Durable («ODD») sont désormais incontournables pour le secteur financier. Cahiers du Centre des Professions Financières,
- ³ Nota: the roundtable was held 15 December 2020, two weeks before the signing of EU – UK TCA
- ⁴ “Joe Biden Picks Boston Mayor Marty Walsh, a Former Union President, as Labor Secretary”, AP, 7 January 2021
- ⁵ Cathy Haye “Devout Catholic Boston Mayor Marty Walsh to Meet with Pope Francis”, *Irish Central*, 17 July 2015 <https://www.irishcentral.com/news/politics/devout-catholic-boston-mayor-marty-walsh-to-meet-with-pope-francis>
- ⁶ J. Murray “Biden Effect: Brits Optimistic 2021 Could Mark Turning Point for Climate Action”, *Business Green*, 7 Jan. 2021 <https://www.businessgreen.com/news/4025501/biden-effect-brits-optimistic-2021-mark-point-climate-action>
- ⁷ Framework for Inclusive Capitalism | Boston University School of Law | March 12, 2021
video: <https://www.youtube.com/watch?v=08FLqcqN38Q>
- ⁸ Gordon, R. J. (2000). Does the "New Economy" Measure up to the Great Inventions of the Past? *Journal of Economic Perspectives*, 14(4), 49-74 <https://www.aeaweb.org/articles?id=10.1257/jep.14.4.49>
- ⁹ Ozawa, T., Castello, S., & Phillips, R. J. (2001). The Internet Revolution, the “McLuhan” Stage of Catch-up & Institutional Reforms in Asia. *Journal of Economic Issues*, 35(2), 289-298.
- ¹⁰ cf. earlier articles by E. Luttwak, or Firzli & Sherry, see also e.g., Gertz, G., & Evers, M. M. (2020). Geoeconomic Competition: Will State Capitalism Win? *The Washington Quarterly*, 43(2), 117-136
- ¹¹ <https://www.businesstoday.in/current/economy-politics/uk-invites-pm-modi-for-g7-summit-in-june/428205.html>
- ¹² **g7 Pensions, 11 June 2021**, registration: esgsummit.org or <https://singaporeforum.org/g7-pensions>