Hurting the planet is not only bad for humanity, it can be bad for business

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When it comes to climate change, one segment of society wants to do good and do well: investors. Be environmentally kind, yes; but build wealth, too. In short, hurting the planet is not only bad for humanity, it can be bad for business. All of which brings pressure to bear on companies that are polluters. How will this shake out? We ask Stephen

Park, an associate professor of business law and the Satell Fellow in Corporate Social Responsibility at the School of Business.

Q: How are investors pressing companies to take action to address climate change?

A: Investors have several different arrows in their quivers to motivate or compel corporations to address climate change. First, we are seeing derivative actions filed by shareholders (essentially suing corporate executives and boards on behalf of the corporation), notably against oil and gas companies such as Exxon, alleging that management has deceived investors about the extent to which climate change poses risks to its business. Second, corporate shareholders can exercise their rights through voting. They can refuse to vote for director candidates to voice their disapproval. Even the threat of a "no" vote can force a company to change its behavior. Third, shareholders can submit proposals for inclusion in the agenda of the annual shareholders meeting. In the U.S., shareholder-proposed resolutions addressing climate change risk, greenhouse gas emissions, and energy consumption have steadily grown over the past few years. Large institutional investors are more and more vocal about climate change risk, and when (investment firms) BlackRock, Vanguard, and State Street start calling for meaningful action and supporting these resolutions, that matters a lot. Even if a climate-related resolution does not pass—and relatively few do—or is withdrawn, it does show that investors are willing to push companies to be more transparent about their sustainability policies, practices, and strategies. And, finally, of course, if all else fails, investors can divest from companies—which aside from selling shares, is often intended to serve as a signal to other investors.

Q: I've read there is research indicating that companies that make significant environmental,

social, and governance (ESG) investments show higher profit margins. Is there evidence of good returns for companies that fight climate change?

A: Yes, there is evidence that various ESG issues—whether we are talking about climate change, labor conditions, or gender equality, to name a few prominent examples—are financially material to companies. Specifically in the context of climate change, companies are incentivized to act for a host of reasons: pro-actively adapting their investment and business strategies before future regulatory mandates force them to (e.g., the stranded assets problem), appealing to socially-minded investors and customers (such as millennials), or making their global supply chains more climate resilient, etc.

However, the big question that we should be asking is how to define and evaluate corporate performance. Now more than ever, I think, there are debates about what the so-called bottom line should be. That's why the Business Roundtable's recent statement re-defining the purpose of a corporation is resonating. People are questioning whether short-term returns and corporate profits should trump the well-being of employees, communities, mom-and-pop businesses along corporate supply chains, and future generations. The benefit corporation movement—for-profit enterprises with legally-embedded social missions—is also part of this growing sentiment.

Aside from the question of corporate purpose, there are substantial challenges in measuring sustainability performance, and in recent years, a number of independent, voluntary, private measurement frameworks have emerged to assist companies. These reporting frameworks—such as standards developed by the Global Reporting Initiative (GRI) and the Sustainability Accounting Standards Board (SASB) – help companies link their environmental and social impacts to financial and operational risks.

Q: How can an individual investor press for action on climate change?

A: There are a lot of new tools! For people like me and you, one option is to buy mutual funds and ETFs (exchange-traded funds) that apply ESG criteria. Impact investing funds actively seek to generate positive social and environmental impacts in addition to financial returns. On the fixed-income side, green bonds are a straightforward way to use your dollars towards earmarked investments in green projects and infrastructure. Social bonds work much the same way for various social investments. If you want to engage with companies on climate change, first and foremost, you can "vote your values" by filling out proxy ballots that arrive in your mail, which increasingly include shareholder resolutions on climate change and other social issues. And new platforms like Say (which works with brokers, companies, and funds to create a clearer dialogue between people and the companies they own shares in) enable shareholders to directly engage with companies.

Q: What are the downsides of companies trying to combat climate change? In other words, won't there be some "losers" as a result of such actions?

A: Investments to mitigate and adapt to climate change will be enormously costly, and any given company will not necessarily reap their benefits in the short term. What I think you are seeing is that companies are grappling with tremendous uncertainty and imperfect information. They don't know the time horizon for sweeping regulatory change (a carbon tax or mandatory carbon pricing, for example). They don't know what green technologies and innovations will take off that might open new markets or facilitate the development of new products or services.

They don't know how changing social values might change how consumers behave (such as the flight shame movement, which tries to pressure travelers to take alternatives such as trains). In my view, the time is drawing closer where all companies—both internally, within their industries, and with government—will have no choice but to address climate change. New firms will emerge and existing firms will be able to transform themselves, but firms that cannot adapt will lose out.

Q: Speaking of unintended consequences, does socially responsible investing increase the risk of a recession, something there appears to increasing worries about?

A: No. In fact, an argument could be made that socially responsible investing, ESG investing, and sustainable finance generally will need to dramatically grow in order to avert the next financial crisis.

Q: Are fossil fuels just plain bad? Or, is there a role for fossil fuels even as investors and others try to fight climate change?

A: This is a hot question for sure! Seriously, in the investor community, there is a schism—or shall we say serious differences of opinion—about whether to exit/divest from all fossil fuel companies or to engage with them through shareholder resolutions and dialogue. Most climate-aware investors are trying to do some of both.

Q: Is there evidence that investor pressure on climate change is having an impact on more than just business—for example, is the pressure causing elected

officials to act?

A: That's the trillion dollar question, right? The future matters, especially when the dire future of climate change looms ever closer. The past couple years in particular have seen a tremendous wave of interest in climate change and other ESG issues in the U.S. – diversity and inclusion, ethical sourcing practices, and the like—that has been led by companies and other private organizations in the financial sector like credit rating agencies and audit firms. States and municipalities across the country are trying to facilitate the deployment and access to private capital for social and environmental purposes by issuing green bonds and establishing green banks (like the Connecticut Green Bank, the nation's first), for example. But after a certain point, there will need to be action at the federal level to regulate and support sustainable finance, such as Sen. Chris Murphy's bill to issue U.S. green bonds and establish a federal green bank. Frankly, the U.S. is falling behind, and our politicians need to help us catch up fast. The magnitude of climate change and its impacts on the U.S. alone is our generation's biggest challenge. Going forward, it is hard to fathom any solutions that do not involve leveraging the enormous pools of capital held by investors, banks, and companies, as well as by governments.

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