Sustainable finance is driving investment for change

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We have a narrow window of time – the next 10 years – to take the decisions needed to alter the trajectory of climate change. The choices made today will determine our future. We have the opportunity to create a new engine for sustainable economic prosperity while preventing the worst consequences of a warming world1. How capital is allocated toward supporting this mega shift is crucial and this trend has been labelled “sustainable finance”. How should corporates and countries embrace this? Considering the recent disruptions and volatility of global energy markets due to the conflict in the Ukraine, energy transition, a key element of sustainability, has become top of mind for many executives. Reducing the reliance on oil and gas as a major source of energy and transitioning towards green or sustainable energy is not just an environmental concern but is becoming a business imperative. In some sort of brutal historical irony, recent tragic events such as the Covid19- pandemic and the conflict in the Ukraine might become a key contributor and accelerant of dramatic change in the energy sector. Sustainability is quickly evolving into a source of competitive advantage for countries and companies.

For organizations to gain this advantage, it is important to shift towards a focus on long term value through embracing the new strategic theme that is sustainable finance.

Public policies supporting this agenda are likely to drive the convergence agenda for those progressive emerging countries and a more affluent world Investment Trends

Companies and their finance functions have increasingly been dealing with the question of sustainability. However, while the costs and regulatory burdens associated with addressing sustainability were quite evident, the benefits of doing so have until recently been less visible and quantifiable. That has changed significantly in very recent times as public awareness of the world's environmental and social challenges has grown and with it the demand for businesses and policymakers to take action. This has risen to the top of the agenda post-COP26 at the tail end of last year2.

A growing body of evidence shows that a focus on environmental, social and governance issues (ESG) only serves to improves companies' financial and operational performance. Deloitte research shows that embracing ESG creates value for all stakeholders and that consumers, employees as well as investors are increasingly seeking greater transparency around ESG related issues3.

Companies across all industries are beginning to recognize this and are making strong purpose-driven commitments and strategic shifts to differentiate themselves in the market. Take MasterCard, which pledged to bring 1 billion people into the digital economy by 20254, or Goldman Sachs, which aims to deploy US$750 billion of sustainable finance by 20305.

An integrated purpose strategy focused on the differentiated role a company serves in society is good business strategy that drives sustainable, long-term value. We have found that 82% of investors agree (35% "strongly agree") that ESG integration will lead to equity outperformance over the next three years. ESG assets are expected to double by 2025 among investors with US$25 trillion in assets. Almost eight in 10 asset managers surveyed globally (78%) incorporate qualitative or quantitative ESG factor assessments into their investmentprocesses6.

A key driving force behind ESG is the increasing launch of funds in the marketplace resulting from demand from both retail and institutional investors. Differentiation in the market will become more important (and more difficult) as many firms are increasing their ESG investment offerings.

As a result, it is expected that by 2025 half of all professionally managed assets in the United States could very well be ESG-mandated assets[7]. It will be difficult for investment managers to effectively compete for capital allocations without a client centric ESG strategy that encompasses credible ESG disclosure and practices. This point is crucial as all investors and regulators are demanding greater transparency and access to more information pertaining to firms' ESG strategies and practices. Beyond transparency toward accountability is an identifiable trend?

By embedding ESG into their strategies, companies are positively influencing their brand, corporate reputation, access to capital, market valuation and their ability to attract talent. This last point is particularly relevant for younger talent seeking employment with companies that embrace deeper societal and an emerging consistent set of global values. A recent study found that 78% of respondents indicated that they would prefer to work for a "purpose-driven" company[8].

Our research reveals that over 2/3 of consumers want to be "in the know" when it comes to understanding how the brands they use embrace ESG issues and they are willing to be more sympathetic toward purpose-driven companies[9]. This observation has become even more prevalent in recent weeks in light of the conflict in the European region and how companies and consumers are responding.

This trend has thus become very evident, and it is apparent that to be a global leading company and brand, a stance on social (and now even political) issues has become an imperative for business.

Corporate management of political activity is undoubtedly becoming more relevant as well as challenging – of course no longer just domestically but internationally.

Sustainable finance and investing into ESG-aligned and ultimately compliant metrics have rapidly moved from niche to the norm. It is now accepted wisdom that embedded ESG in corporate business strategy and operations is essential to successful capital allocation and utilisation. How countries regulate the rapidly arising sector will also serve as a competitive national advantage.

How public policymakers craft a regulatory environment that best enables the growth of ESG capital markets in their respective countries will be a key defining trend in the years to come.

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