ESG BECOMES MANDATORY

THE *2030* FORECAST

Ten ways our human civilization will come to grips with the forces it has unleashed

Ogilvy CONSULTING

Introduction

ESG has become a political punching bag, but while businesses have to pay heed to the political environment in which they operate, they have an overriding duty to their customers and stakeholders. It's because of them that ESG isn't going away. In fact, it's rise has just begun.

That said, the easy days are over. New oversight is coming to ESG reporting, and it is accompanied by powerful market pressure to manage companies in a socially and environmentally responsible way. This isn't "woke capitalism," whatever that pejorative means; it's good business. ESG-oriented companies perform better and are better aligned with the values of their customers, at least in the main. No matter the industry, businesses will not be able to escape thoroughly transparent ESG review, and it's time to put in place the structures to make that process produce a positive outcome.

Short-term thinking has never been a prudent way to grow a business or brand.
Ogilvy Consulting has identified 10 macro shifts and major inflection points effecting world politics, global economics, the future workforce, health and wellness and ESG.

The 2030 Forecast helps prepare business and brands for these major global shifts, with critical insights for our clients to help plan for the future.

For the full report go to:
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THE *2030* FORECAST

Environment, social, and governance (ESG) measures have been ubiquitous—but not yet meaningful. The absence of standards and enforcement has led to greenwashing and a devaluation of the entire ESG concept, which is not too surprising for an emergent trend that has new costs. Climate change targets are not yet optimized—especially if we want to keep Earth habitable. ESG will become a corporate priority, but like the crypto business, it will need metrics, standards, and independent oversight.

A Controversial Metric Gets Real

For a few years there, the hottest investing club in New York (and elsewhere) went by three initials: E, S, and G. They stand for environment, social, and governance and describe a poorly defined set of reporting principles aligned to the United Nations Sustainable Development Goals (UNSDGs).

BlackRock led a crusade of investor money flowing into companies that measured and reported on their ESG progress, but as the tide grew, so did criticism. Those eager to see real progress on diversity, equity, and inclusion and aggressive climate action decry the absence of regulation and standards. To them, ESG reports just supplied the means to paper over business as usual. ESG also became a target in the culture wars, with states like Florida and Texas enacting punitive anti-ESG laws and divesting from firms that prioritize ESG. They maintain that these principles are just another manifestation of "woke capitalism" and an attack against fossil fuels. Businesses, the argument runs, have no place in making decisions that have any political flavor.

Despite the headwinds, ESG will only gain steam between now and 2030. Universal standards and regulation regimes will answer criticisms of greenwashing while revanchist attacks will keep grabbing headlines. And yet underlying progress will continue. Florida may have divested $2 billion from BlackRock for political reasons, but that's not going to deter a company with $8 trillion in assets under management.

Here's why the movement toward accountable ESG is unstoppable: it works. An NYU Stern School meta-analysis of over 1,000 studies found a definitive positive correlation between ESG and financial performance—a trend that becomes more pronounced over time. The meta-analysis also found that managing for a low carbon future improves financial performance, while an ESG focus for investors protects against downside risk. McKinsey's analysis produced similar results, and its analysts delved into the ways ESG can boost financial performance.

McKinsey analyst Robin Nuttall notes that a better ESG score lowers the cost of capital. It also boosts top-line growth. Nuttall says, "If you are a consumer goods company with a stronger sustainability proposition, you are more likely to attract customer loyalty and new customer segments. There is evidence that brands with more sustainable impact grow faster than brands that have a less sustainable proposition." Improved ESG efforts also use resources more efficiently, lowering costs in the process and reducing the risk of stranding assets. It reduces regulatory exposure, and, Nuttall reports, "newer recruits and millennials demand purposeful work and if you are an employer that can meet that need, you will attract and retain that talent, and likely higher productivity in the workplace." That's a quantifiable benefit, too—one that can add approximately 2% annually to a company's stock price, McKinsey reports.

DE&I IS ESSENTIAL FOR ATTRACTING AND RETAINING TALENT

76%

of US employees and job seekers consider a diverse workforce important when evaluating employment

32%

of US employees and job seekers would not apply to a company that lacks diversity

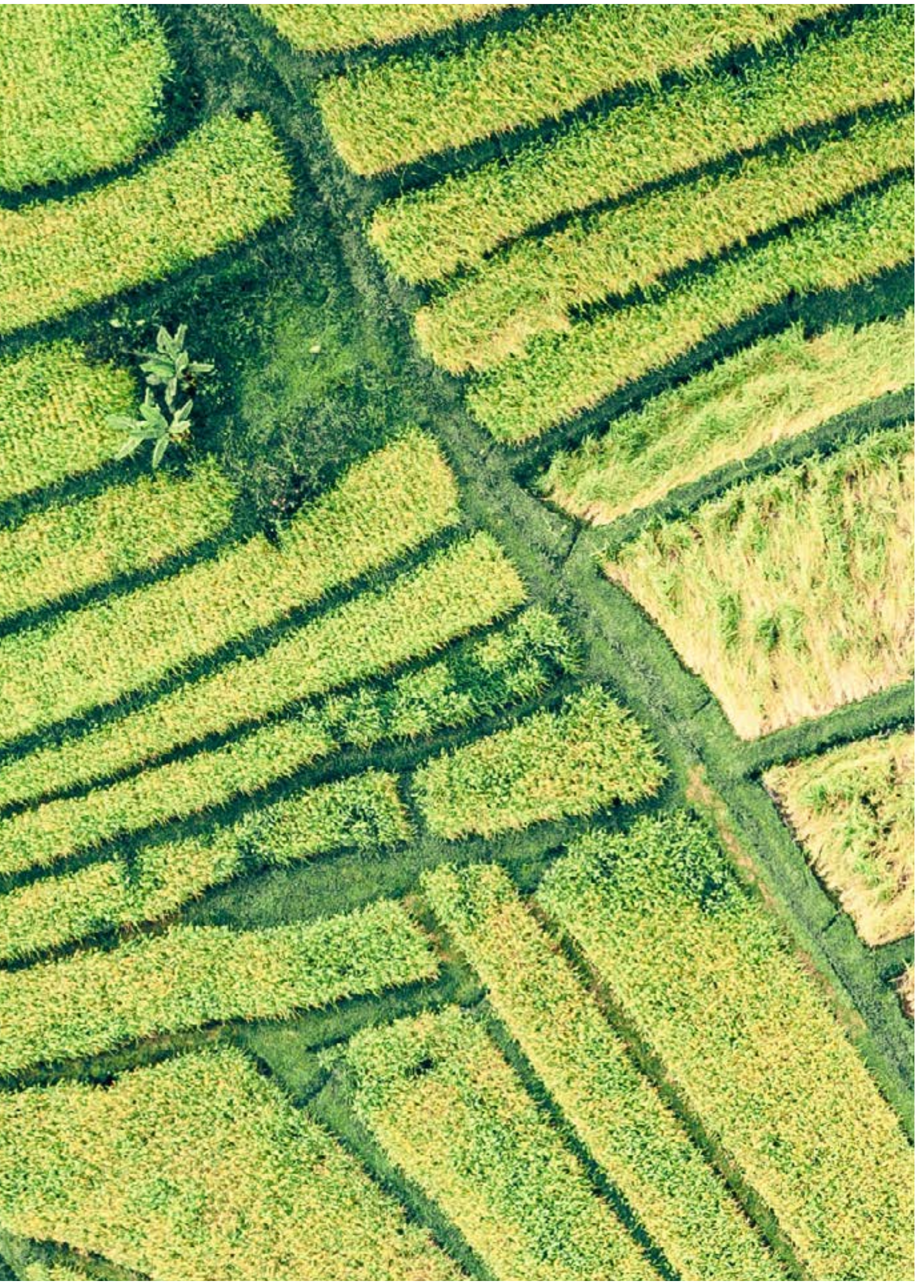
41%

of US employees and job seekers have quit a job after witnessing or experiencing discrimination at work

Source: "Diversity & Inclusion Workplace Survey," Glassdoor, 2020.

DE&I is also a growing industry. States like California are spending big on DE&I initiatives—so much so that the Center for Organizational Research and Education reports that it "is easily worth $1 billion in Golden State spending."

Major pushes are happening at the national level, too, with federal officials working on a strategy for DE&I policies for the government, which, it is hoped, will provide a framework for companies and organizations nationwide.



Real Metrics

ESG has been hampered by a lack of transparency and inconsistent metrics, and that's fueled the backlash. However, calls for universal, effective, and consistent standards are growing around the world. Brands that once advertised themselves as environmentally and socially responsible without third-party verification are seeing the party end. Given the financial benefit that accrues to companies with good ESG performance, subpar efforts masked by greenwashed reports are nothing short of financial malpractice.

The unmistakable, urgent, and present reality of climate change takes sustainability from a value to promote to a mission-critical outcome. Investors and regulators have dialed up scrutiny and demanded transparency and effectiveness—and not just because they see the impacts of climate change firsthand. Instead, the externalities of a warming world are forcing businesses to recognize that "sustainability" now means remaining in business. Absent efforts by individual businesses and industry as a whole to decarbonize, the existential threat posed by climate change will shutter—and shatter—the global economy.

Business leaders are feeling the heat: 58% of CEOs are under increased pressure for ESG reporting and transparency. The EU, at least, has responded, implementing a new ESG framework called the Corporate Sustainability Reporting Directive (CSRD). The CSRD will require many more companies to engage in ESG disclosure and begin the process of building consistency in reporting. After all, to sustain is to last.

Good COP, Bad COP

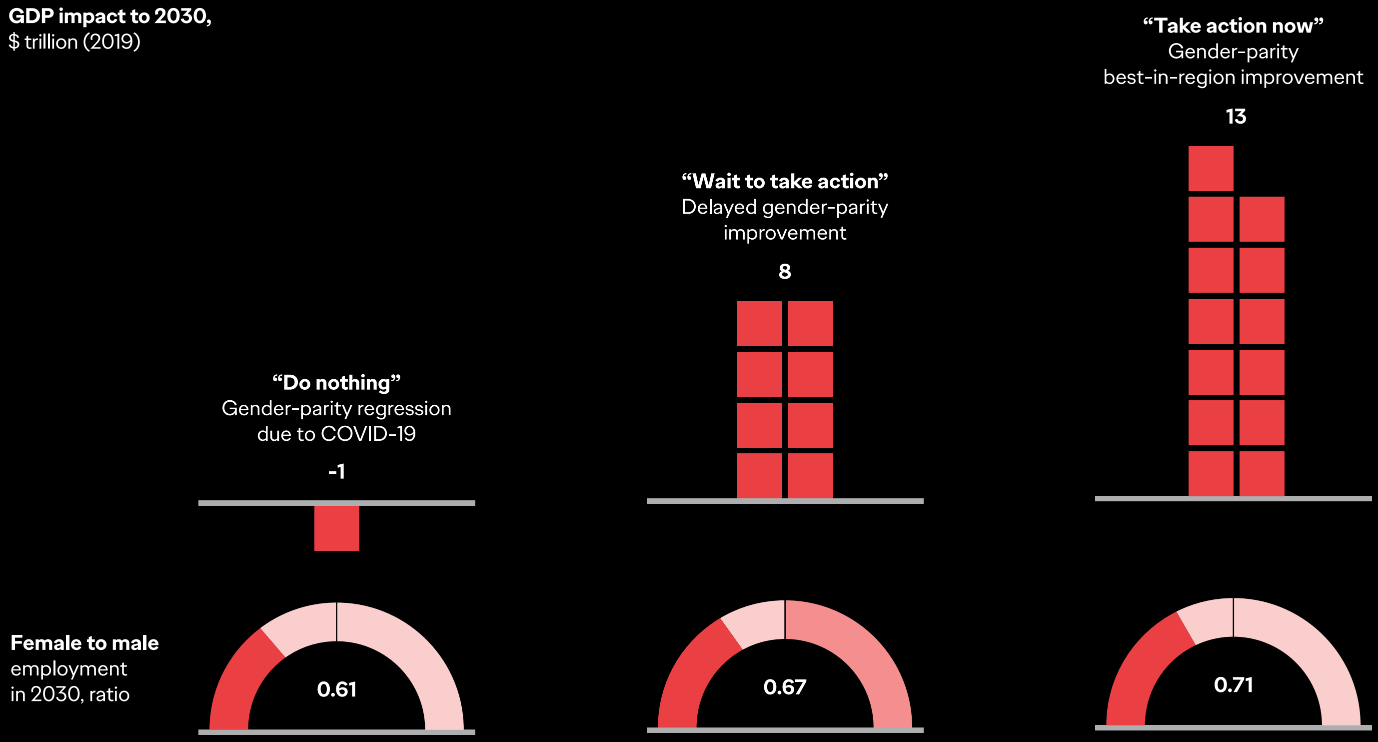
A dose of reality is in order. Society has been talking about curbing emissions for three decades, since the Rio de Janeiro Earth Summit, and, as Elizabeth Kolbert writes in the *New Yorker*, "at some point during all the 'blah, blah, blah'-ing—it's hard to say when, exactly—climate change ceased to be a prospective problem and became a clear and present one." Humanity will not dodge this bullet, even as leaders convene COPs and "speak loftily about 'net zero' and a 'low-carbon economy.' But nothing will change, and, as a result, everything will change." The impacts of that are frightening—crop failures, aridification, inundation, conflagration, and, finally, migration. Kolbert points to economic anthropologist Jason Hickel, who points out that, as a product of capitalism, climate change can't be solved by the same solution.

That's crap. Capitalism, especially the poorly regulated late-stage variety, has plenty of problems both practical and moral, but if it is anything, it is this: an exquisitely skilled survival machine. Businesses are starting to take planetary issues seriously, albeit way too late, because shareholders and stakeholders are concerned about sustainability—for the businesses they are invested in and for themselves. And so ESG will thrive for years to come because it will become an essential metric to evaluate a business's future potential.

Act Now

Delaying efforts to achieve gender parity will cost the global economy $13 billion. Companies with larger numbers of women executives outperform those with fewer (or, sadly, none), according to a landmark McKinsey study. The effect is even more pronounced for ethnic diversity.

INCREASING GENDER PARITY IN THE WORKPLACE PAYS OFF



Source: "COVID-19 and gender equality: Countering the regressive effects," McKinsey Global Institute, 2020.

Build sustainability considerations into business decision-making. Policy is an easy solution, but it won't create enough change on its own

The implications should be obvious. Build a diverse talent pipeline. The one already in place isn't good enough, and any honest business knows that a diverse workforce helps companies understand, reflect, and relate to a diverse world. Structural issues are real, and any technical business needs to invest in secondary and postsecondary scouting and preparation lest great talent never get the chance to enter historically closed industries. The societal costs of that are clear. The financial ones to an individual business should be, too. And make sure your workforce knows. Talent is looking to remain at or join companies that are DE&I leaders, but data from Glassdoor shows that two-thirds of employees and applicants trust DE&I reports from a company's workforce the most.

Build sustainability considerations into business decision-making. Policy is an easy solution, but it won't create enough change on its own. Inculcating the behaviors in management, however, will. While making executives accountable for the sustainability of their areas and tying compensation to their success may be more complex, it will also be more effective. Every business needs to recognize that it is part of an industry ecosystem; individual actions can spur good behavior in competitors and suppliers. In fact, a supplier code of conduct or a sustainability imperative can decarbonize an entire supply and value chain.
Don't wait on verified ESG reporting, either. Businesses should get behind efforts to regulate and regularize disclosures. Engage third-party auditors if standards are not in place. Better yet: build an industry coalition to set them and work with local authorities to get them codified. That's part of the "G" in ESG, but there's much more to that heretofore neglected letter, like respect for shareholders, operating in the public interest, and planning and acting for the long term.

Inherently polluting industries need to take heed, too, since the expense of carbon offsets and carbon capture is sure to balloon. The carbon trading market is growing fast. In fact, it grew by 164% in 2021 alone, and prices are on an upward trend, too. Net-zero policies will also goose carbon-offset markets—and prices.

Given the oft-reported propensity for consumers to buy from companies that share their values, companies need to market their ESG. Since many companies have proclaimed themselves to be good corporate citizens while failing to follow through on public commitments, skepticism reigns among consumers and investors. Nevertheless, the brands of the future will rest on a foundation of sustainability. Build that brand incrementally—in conjunction with progress on ESG.

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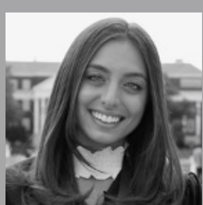

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