EPILOGUE – THE INTERVIEWS

Now that you have read what I have to say about ESG and the role of business, I thought it would be useful to test the hypothesis of the book with a few experts. I deliberately decided not to interview current CEOs or corporate executives for two reasons. First, the internal process for securing approval for the final text would be formidable. Second, even after navigating the afore-mentioned process, it is questionable if the companies would have something interesting to say. Being a former corporate propagandist myself, I can assert with some confidence that companies cannot resist the temptation of staying on propaganda on a contentious issue like ESG. All of this makes me a cynical person I know, but I decided that the best option would be to interview people who once served in senior roles in corporations and are now somewhat removed. In terms of process, none of the interviewees reviewed the manuscript before the interviews, enabling them to speak freely about the issues.

Vasuki Shastry

V. SHANKAR

I first met V. Shankar in Bombay in 1985, when I was a pesky journalist for a business magazine, and he was a rising investment banker. He is a Cofounder and Chief Executive Officer of Gateway Partners, an emerging markets-centered private equity fund domiciled in Singapore and Dubai. Prior to Gateway, Shankar was CEO – Middle East, Africa, Europe, and the Americas, and a member of the global board of Standard Chartered Bank Plc and held senior roles in America and Asia at the Bank of America. In the spirit of full disclosure, I am an ESG Advisor for Gateway Partners.

Q. As a manager of an emerging markets-centered private equity fund, how relevant and realistic are the evolving global ESG standards in your investment footprint?

A. First thing I would like to say that we are all starting off, to use golfing analogy, with different handicaps. Developed markets are like Tiger Woods and developing countries are amateurs. Their fiscal and financial capacity is substantially different so taking a one-size-fits-all approach is a problem. Is this a global problem that we all need to resolve and converge? The answer is a resounding yes. The question is the pace. If you look at the previous commitments made by the west to support emerging markets come up to speed, more than 80% of the commitments by some calculations have not been met. Emerging markets need help, albeit emerging markets are a vast swathe of territory. Some of them, China, and India for example, are well equipped to handle this financially. On the other extreme, you have poor African countries like Burkina Faso and its peers who lack the financial, operating, and technical capacity. They need support and whatever commitments will be made this time around can't just be bark and all talk, they need to be tangible and have a bite.

Q. How do you ensure this?

One possible way of ensuring commitments have bite is for countries being able to pledge IMF-issued SDRs (special drawing rights) as collateral so that the funding is available through a multilateral institution like the IMF or World Bank rather than relying on the good graces of governments which often change in democracies. We have seen commitments made by one administration reneged by another coming into power for whatever reason. Overall, emerging markets need time to fully comply with global ESG standards. My suggestion would be for a system akin to "handicapping" in golf where countries which are further along the journey should not go for net zero by 2050 but should probably do so by 2035 or 2040. Those countries which are substantially behind should have the climate space until 2060. So hypothetically, the whole world gets to net zero by that extended period. Developing countries need the financial and policy support. The other challenge is how we are measuring this. This is not refined mathematics where one plus one equals two. We can make these metrics so complex that we will all drown in it and merely stuff the pocket of consultants. By making it complex, we also make sure that the dice is loaded in favor of the larger firms. This is because they alone have the capacity, financial or technical, to measure and to report. Let's not make perfection the enemy of the good.

Q. You mentioned an extended period of net zero compliance for emerging and developing markets? What are some of the immediate challenges they face in getting started?

A. We need to fundamentally understand that there are trade-offs which represent the broader challenge you are alluding to. There are trade-offs between the creation of jobs and the environment, between governance and the social implications. You can see these trade-offs being discussed even in advanced markets like the United States. We need to also recognize that who sets the standards is an issue. For instance, on governance, we have somehow implicitly accepted that the western, Anglo-Saxon governance model is the best. That has not necessarily proven to be any better than many other forms of governance. Western boards are still stuffed with male, pale, and stale people. There have been flaws exposed in developed markets, as much rigging of the markets there as anywhere else. So how we go about setting standards and making sure all voices are included is important.

Q. As an asset manager complying with global standards, are you able to shape and influence the behaviors of the firms you invest in?

A. The answer to "are we able to influence" is yes. But implicit in that answer is that you don't want to be pushing water uphill. You want to invest in companies and managements that fundamentally believe in ESG and being a good corporate citizen. You cannot be selling fire insurance to an arsonist. Our philosophy is to invest in companies and managements that are committed to being a good corporate citizen and believe that by improving their "E", improving their "S", and improving their "G", they will benefit. There are also several good reasons why this approach is good. First, the DNA of the promoters of the business is an important investment consideration. Second, you don't want to be investing in something which will become a stranded asset. It could become stranded because it is going to be disrupted by a green-tech firm or somebody who is a better corporate citizen. You could get stranded because of changing consumer preference because of regulation. So, for all the reasons cited above, it is both a defense and offense strategy to incorporate ESG into your capital risk. However, let's not get carried away by extreme voices on either side of the debate. There is a role for moderate voices and for taking a calibrated approach because one size will not fit all.

Q. What would be an example of such a calibrated approach?

One good example is cement. One could argue that if cement were a country, it would be the third or fourth largest polluter in the world and therefore you should cease all production. But cement is a fundamental pillar of development. Should we say that Africans should not have cement and live in thatched huts. Or should we only use green cement which is going to cost multiple times as much as the traditional product? The answer is Africans need access to as much cement as they need because they are only now starting off on their development journey. This is to balance and nuance the issue between job security, food, development, and simultaneously tackle climate change.

Q. In your investment footprint of Africa, the Middle East, and South and Southeast Asia, there is a mix of developing and developed markets. Are there regional variations and can companies learn from each other in implementing better ESG standards?

A. This may not be music to everyone's ears. Al Gore became a missionary to promote climate change. But without China we would not be having the affordability in terms of solar or wind power which we are all enjoying today and has become a real alternative to fossil fuels. We can also talk endlessly about electric vehicles, but you must consider that two-thirds of EVs made today are in China. China seized this opportunity and is way ahead of the curve, and other emerging markets can learn from them. A quick follow-up is India, which was initially resisting the climate change debate and I have been in meetings where they said that we have coal and that is the cheapest form of energy. Now that the cost curve has changed, where solar can be produced almost at parity, India has become a big convert. It also becomes a business opportunity if you do it at scale. So, no we don't need to look at this just as a challenge. Then countries like Singapore and UAE come to mind which are further along the journey. So, the upshot is we don't need to necessarily learn from the United States or Europe.

Q. So as a corollary, the sustainable finance opportunity world-wide is so significant, are we getting preoccupied with achieving net zero targets?

A. It's a journey. We should have milestones along the way in terms of how we are progressing toward the goal. Reducing emissions by 50% is as effective as someone launching a new venture where the emissions footprint starts off at that level. That is the equation we need to work. So, coming back to cement, if we can find a way of reducing emissions by process improvements or alternative fuels, that is as good as or even better than building a new plant with 50% less emissions.

Q. As a former banker and current asset manager, do you see sustainable finance flourishing in the next five years in emerging markets?

A. Yes, finance can flourish but it is a follower. What creates the need for sustainable finance is a green project. You want demand to be created and there will be more green projects because of regulatory and societal pressures. The cost curve for green solutions also achieving parity with traditional fuels is also an important part of this equation. Which is why I believe that despite a lot of talk about hydrogen as a viable fuel or that of solid-state batteries, their commercial viability is not tested yet absent huge government subsidies. These will require time and investments in scale and technology, just as it took solar to achieve viability. Governments can indeed influence scale and adoption. Not just through subsidies but also through "industrial policy" which is anathema for die-hard believers in free markets! What President Biden has done through the Inflation Reduction Act (IRA) is effectively a new form of industrial policy at work. The last thing I would say is that we need to battle against our approach being hijacked by extreme voices. We also need to shut down "energy hypocrisy." It is ok for Europe to use coal but not ok for some emerging markets. It is ok for the United Kingdom to have gas and oil pipelines, but if Africa is doing it in Uganda or Tanzania, it is a problem and financing is not being made available. These are sheer double standards and hypocrisy.

DENIZ HARUT

Deniz Harut was my colleague at Standard Chartered Bank, where her primary focus areas were sovereign advisory and sustainable finance. She is *currently an Executive Director of Pollination, the London-based specialist climate change investment and advisory firm. As the interview will demonstrate, Deniz is a thought leader in sustainable finance and has broad expertise in emerging markets, development finance, and in advising companies on net zero strategies and in navigating the climate transition.*

Q. How do you concretely assess net zero plans of major financial institutions and the related concerns over companies postponing difficult decisions?

A. The direction of travel is clear, and the private sector has been quite decisive. Financial institutions (and markets) are reengineering their business models and integrating climate considerations and the broad potential impact. The drivers are two-fold. In the United Kingdom and the EU, it is the regulators who are providing the advanced push. Simultaneously, pressure has also built up from asset owners and institutional investors. We are also seeing shareholder activism on the rise and are observing more management teams being challenged on climate inaction. It has been a top-down process and understandably there will be leaders and there will be laggards.

Q. You mentioned that the push for greater disclosure is coming from financial regulators. How is this impacting the financial sector in terms of how they are preparing themselves for greater compliance?

A. The Taskforce for Climate Related Disclosures (TCFD) has become mandatory in many advanced jurisdictions. This has created a rush among financial institutions to get the right data and to address any immediate gaps or weaknesses. There are two elements to this challenge. First, banks and asset managers want to ensure that they are across the line when it comes to full compliance with the regulations. Second, some institutions are using this opportunity to completely reengineer their business models. They want to go beyond integrated reporting and figure out how they can thrive in a global economy which is decarbonizing, including the adaptation of new technologies. I am also seeing this in private markets and what is accelerating the process is the availability of shadow ratings on how a company is performing in terms of climate and nature impacts. At the end of the day, there will be winners (alpha) and there will be many others who will remain stagnant. I am encouraged that companies are taking a holistic approach and no longer looking at the climate challenge through the narrow lens of data management or risk approaches.

Q. You mentioned adaptation of new technologies in the climate and green space. Is that having a tangible, positive impact in accelerating the climate transition?

A. Most certainly, yes. There is a huge pipeline of venture capital in the climate-tech space which is becoming more visible and impactful. The most impressive aspect is it is taking place across the board and markets are also taking a view on pricing. The critical challenge is in building the adaptive capacity to facilitate the transition. So, you have entirely new ventures in carbon markets, in capturing carbon data and you are likely to see the emergence of many unicorns in this space.

Q. This is all encouraging but what about the capacity of C-suites and Boards? Are they well prepared to embrace the challenge and steer their companies on to the green transition?

A. There needs to be a shake-up. The fundamental challenge, when it comes to Boards, is the lack of diversity and expertise in understanding emerging challenges in the environmental and social sphere. Boards are well equipped to handle traditional financial and risk management issues concerning a business. The climate challenge cannot be reduced to these two issues because it has a much broader societal impact. Similarly, CEOs and C-suites are not climate experts, and you need to bring in more of them to advise companies on the transition. Rethinking the Board and management skill sets is going to be quite the challenge.

Q. The ESG space, as you well know, has been consumed with allegations of greenwashing. Do you feel that the sector will recover from what appears to be a series of severe setbacks?

A. We should place this in the appropriate context. Environmental and social issues are a legacy of the global financial crisis – where financial institutions were found to be badly managed, and some were also guilty of selling unethical financial products. The regulatory regime which was established in the aftermath of the GFC has led to a rewiring of financial services and a much more stable and healthy system. In the current context of greenwashing, we are bound to make mistakes but are better positioned to learn from them. There are several positive factors which are converging to address greenwashing. This includes strengthened ESG regulation on issuers, intermediaries, and the rating agencies themselves. We also need to get smarter at due diligence and there is a huge burden on companies which don't have the right data. Regulatory consistency is another important factor, and the work being carried by the Sustainability Accounting Standards Board (SASB) in updating the IFRS regulations as well as the EU taxonomy for sustainable finance will enable this process.

Q. A final question on whether the "S" component of ESG is getting crowded out as business is primarily focused on the climate challenge?

A. There is an element of climate overshadowing the social and governance aspects of ESG. But it is a logical journey – we should effectively deal with emissions first and the other aspects will follow. The focus on nature risks, for example, is an integral part of the "S" pillar because it has huge implications on the habitat and for disadvantaged communities. Diversity and inclusion, as I noted earlier, must be rethought. It is not simply improving diversity in C-suites and Boards but also to ensure that the voices of women and minorities, who are at the frontline of climate distress, are heard and acted upon. The financial sector can contribute by innovating on how we drive financial inclusion. Could we, for example, consider originating carbon credits for local communities and gender empowerment. This will be the true metric of impact investing.

NICK LOVEGROVE

Nick is currently Professor of Practice at Georgetown University's McDonough School of Business, where he teaches courses on management, strategic problem-solving, and principled leadership. I occasionally deliver guest lectures in his classroom. Prior to academia, Nick had a rich and diverse career in consulting (McKinsey & Co, where he was Managing Partner of the D.C. Office, Albright Stonebridge, and Brunswick), public service (he was special advisor to former UK Prime Minister Tony Blair), and in communications. Nick is the author of a fascinating book The Mosaic Principle,[1] *which argues that life – professionally and personally – is*

[1] The Mosaic Principle: The Six Dimensions of a Remarkable Life and Career – Nick Lovegrove, Public Affairs, 2017.

lived to the fullest as a mosaic, encompassing a rich and complex set of diverse experiences.

Q. In your under-graduate and graduate classroom, is there significantly greater interest from students on ESG and climate issues and how are universities adapting?

A. I would say yes and frame this as an issue of meeting demand. There is of course a recognition that climate change is the key issue of our time and educators are adapting to ensure that this is integrated into our undergrad and graduate level courses. It is at the same time hard to know if all the demand is met, and this is an ongoing process of integrating environmental and social issues into our curriculum. The business school, for example, has initiated a graduate-level degree in sustainable development.

Q. Is there a clear sense in the student population that ESG issues are core or central to what they will learn?

A. They are eager to learn but of course the student community don't come with high knowledge about the issues. They are not experts, which is not surprising, but want to learn. From what I see in the classroom, this is not an activist generation. One should not generalize because student interests differ based on the program they are pursuing – those pursuing a business degree will have different views compared with students studying foreign policy. Two general observations from me. First, in the American context, the killing of George Floyd in May 2020 ignited an emotional energy about diversity and inclusion issues which is still resonating. This is not necessarily seen as an ESG issue per se but something that our students are passionate about. Second, I have not observed an antipathy toward the establishment, in this case the university. The students are here to learn but they recognize that there are bigger social issues which they are committed and passionate about.

Q. So you don't see this student generation to be in the mold of say their rebellious predecessors of our era?

A. As I noted earlier, there is no student antipathy toward the system and no simmering discontent. One must be careful in drawing sweeping conclusions given their backgrounds and the institution they are studying in. Like every generation, they are driven by career aspirations, but I am confident that when faced with a challenge, they will change.

Q. You were a consultant for much of your career. How radically different is your new job as a professor?

A. There are commonalities and sharp differences as well. For one, there are close interlinkages as they belong to a single ecosystem. However, the personal challenges are different. In teaching, the opportunity is in shaping perceptions, influencing behaviors, and in effect building the leaders of tomorrow. In consulting, there is a difference in methodology and approach of course and there is a constant need to meet market demand with new services through an adaptive business model. I attempt to connect my students to the world of consulting in my classes, providing a glimpse into how business works. Academia is difficult to change because at the core we are bound by the special knowledge of the faculty. It is much more supply and academic lead. The next decade, particularly in America, will shake up universities. There will be a decline in the volume of the incoming student population (due to demographic challenges) and nonelite schools will suffer, as they will have less material resources and agility compared with more established institutions. **We need to build much more robust foundations.**