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Preparing for a dramatically different future

The bandwagon of stakeholder capitalism and sustainable finance is truly in motion, and those not already on it it risk getting left behind

TO QUOTE Singapore's Senior Minister Tharman Shanmugaratnam from his national address last month, "the future begins now".

That future will be dramatically different not only for governments and individuals, but also for big business and big finance. What Covid-19 has done is accelerate the disruption already heralded by the fourth industrial revolution and demographic trends, and underscore the urgency required to address systemic vulnerabilities.

The global economy was not exactly fighting fit when this tragic pandemic hit us. The trade war between the United States and China had only just entered a form of awkward truce, the US Federal Reserve and the European Central Bank had already started reversing their interest rate hiking cycle, and the International Monetary Fund's growth forecasts had already undergone multiple downgrades.

The immediate macroeconomic policy response was swift and decisive around the world. So much so, that they have seemingly overturned several taboos.

Changed mindsets

Who would've thought, in the wake of a polarised election campaign in the United Kingdom, that the Conservative Chancellor (a former Goldman Sachs executive) would announce that for the first time in history, "the government is going to pay people's wages", earning praise from the trade union movement?

In countries ranging from Canada to Japan, non-discriminatory cash disbursements looked like temporary versions of Universal Basic Income – no questions asked. On the monetary front, central banks increased the scale and scope of assets that they purchased, bringing interest rates down to record lows across all maturities.

Printing money without concern for inflation or even direct monetisation of government debt now appear to be legitimate instruments in the policy toolkit. The financial system is flush with cash; traditional capital markets are arguably overvalued.

We have also changed our minds about hyper-optimised, cost-efficient supply chains. As governments scrambled to secure food and supplies of healthcare and other essential products, we realised that a bit of duplication and diversity are desirable for sustainability of the system. Cost-cutting measures no longer signal higher returns in an unequivocal way; they might indicate latent risks and reduced resilience.

It is early days, but individuals are also showing tremendous agility and open-mindedness in pivoting from old to new roles – from airline crew to healthcare service, hotel hospitality to retail management or taxi driver to food delivery for example.

Changing mindsets, challenging "sacred cows" and established habits, and embracing fundamentally different roles are the hallmarks of the post-pandemic world.

Stakeholder capitalism and inclusion

It is almost a year since the Business Roundtable, whose members are chief executives of major US companies, issued a path-breaking declaration on the purpose of a corporation: to serve all stakeholders, moving away from shareholder primacy.

In the following months, the UN Global Compact, UN Environment programme, the World Economic Forum, the Organisation for Economic Co-operation and Development, various central banks, and major multinationals stepped up their commitment to mobilise private-sector resources towards the sustainable development goals.

However, there was legitimate scepticism about the sincerity with which companies would back their rhetoric with action. How much of this is window-dressing, tokenism, or impact-washing?

Covid-19 presents a powerful threshold-moment in the alignment of words with deeds.

To take two examples from Singapore, both DBS and UBS have made commitments with regards to jobs and skills. Through the Singapore UBS Program for Employability and Resilience (Super), the Swiss bank will create 300 new jobs which is the equivalent of 10 per cent of its workforce in the country. At the same time, South-east Asia's largest bank DBS announced its commitment to hiring 2,000 people, at least half of whom will be in new roles.

How are these measures justified from the perspective of return-on-equity when the outlook for earnings is so murky? Members of the C-suite will admit that in the current economic environment, the first instinct is to cut back on hiring and costs in general.

However, if you have an entire cohort of fresh graduates coming out of higher education without jobs, that simply cannot be good for business. The self-enlightened realisation is that an economy is a circular flow of income; that flow does not function without adequate demand. In the fullness of time, responding to the social need of the hour is simply good business: stakeholder and shareholder interests converge.

More generally, companies need to help sustain demand for their products. In a world of widening inequality, income flows to those who consume less and save more. Demand must come from new sources – new communities, new regions, and new markets. As a result, inclusion becomes a strategic driver of growth.

For example, the education group Pearson recently issued what it claims to be the world's first education-linked social bond. The proceeds of £350 million (S$611.1 million) can only be used to deliver online education to "underserved learners and communities, including those from low-income backgrounds, with disabilities and the unemployed".

Sustainable investing and inclusion

What is true for investee companies is also true for investors of capital. Existing assets and entire asset-classes are saturated, the outlook for returns is low, and interest rates are expected to remain low for an extended period. The wall of money released by quantitative easing needs new destinations.

Here again, inclusion is the way out. New securities and asset classes will have to be created. The finance industry now has a commercial and existential impetus to rapidly bring the field of "responsible investing", green finance, social bonds etc into the mainstream.

More money should flow into previously excluded sectors with significant impact on the real economy. For example, in some emerging economies, this could mean deeper and wider capital markets which in turn would foster domestic insurance and pension services.

Elsewhere, government support for localised micro and small enterprises could be magnified by crowding in private investors who are looking for new avenues to deploy their funds.

Large influential investors such as sovereign wealth funds can lead the way. In recent weeks, Singapore's GIC has underscored long-term themes such as environmental, social and governance (ESG) factors as well as the importance of bottom-up opportunities versus top-down views.

The largest pension fund in the world, Japan's GPIF, is also taking a "systems view" of the investment landscape, demanding ESG awareness from all of their asset managers and catalysing inclusion. The fact that GPIF posted record losses of US$164 billion in the first quarter of 2020 might suggest that investors of their size have simply run out of opportunities in the current universe of assets. It is in their own interest that they should help expand that universe.

Jump on the bandwagon

The investment profession is also shaped by customer preferences. The recent trust survey conducted by CFA Institute shows that increasingly, the beneficial owners of funds wish to see how their returns are generated. They seek greater information, innovation, and influence to make sure that the pursuit of economic value is consistent with their values.

Financial advisors and investment managers need to be honest about the long-term outlook of investments so as not to erode trust if and when investment performance falls short of expectations. That dialogue must include ESG factors.

Finally, regulators are also nudging in the right direction. Disclosure directives in Europe, stress tests required by central banks such as the Bank of England, the active ongoing debate about reporting standards – all point towards an inflection point.

The bandwagon of stakeholder capitalism and sustainable finance is well and truly in motion. As the future unfolds, those not already on it – authentically and materially – risk getting left behind.

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