

# The Case for Responsible Business and Investing Practices

## Why Environmental, Social & Governance (ESG) Factors Are Good for Business

Responsible business operations and investing are no longer optional but essential for long-term financial success. Incorporating practices that include environmental, social, and governance considerations (ESG) positions businesses to navigate the challenges and opportunities arising from climate risks, evolving regulatory landscapes, and stakeholder demands. **For long-term viability, American businesses need the freedom to operate responsibly.** Yet, the freedom to consider ESG risks and impacts is under attack, fueled by special interest money and political culture wars that have nothing to do with protecting Main Street businesses. These attacks must be met with resistance. When policymakers protect business and investor freedom to operate responsibly, responsible practices become a core corporate strategy and foster a more resilient economy.

### ESG Business Benefits At-A-Glance

#### Boosting Investor Confidence and Return on Investment

U.S. investing trends reflect a growing preference for responsible business practices:

- ❖ In 2022, 60% of sustainable U.S. large-growth funds have steadily ranked in the top half of the Morningstar U.S. Growth Index; and sustainable equity funds outperformed non-ESG peer funds by a median of 4.3% in 2020.<sup>1</sup>
- ❖ Morgan Stanley reported that in 2023 – a year riddled with volatility and recession – funds focused on “environmental, social and governance (ESG) factors, across both stocks and bonds, weathered the year better than non-ESG portfolios.” Sustainable funds had a return of 6.9%, nearly double that of traditional funds’ 3.8% rate of return.<sup>2</sup>

#### Meeting Consumer Demand

Nearly two-thirds of younger consumers seek to support sustainable brands, and these evolving consumer preferences are attracting crucial financial support from private equity investors.<sup>3</sup> In 2021, 99% of Millennial investors in the U.S. expressed interest in sustainable investing, signifying a generational shift where investors seek both financial returns and positive societal and environmental impact.<sup>4</sup> The financial capital that is becoming available to this generation gives them the power to ensure that responsible business practices are a priority. This power is reshaping the financial industry, prompting fund managers and financial institutions to expand their offerings of ESG-aligned investment products and creating more demand for companies to embrace responsible business practices.<sup>5</sup>

<sup>1</sup>Sustainable Funds U.S. Landscape Report (n.d.). Morningstar. <https://www.morningstar.com/lp/sustainable-funds-landscape-report>

<sup>2</sup>Sustainable Funds Beating Peers in 2023 (2023). Morgan Stanley. <https://www.morganstanley.com/ideas/sustainable-funds-performance-2023>

<sup>3</sup>Sustainable Investing: 10-Year Outlook. (2023). Morgan Stanley. <https://www.morganstanley.com/ideas/sustainable-investing-10-year-outlook>

<sup>4</sup>Ibid.

<sup>5</sup> Ibid.

### Mitigating Climate Risks

Climate change presents new risks to business operations; managing those risks is critical to long-term success. Forty years ago, the U.S. averaged one (inflation-adjusted) billion-dollar disaster every four months. Now, there is one every three weeks, on average.<sup>6</sup> Climate-related damages are projected to further reduce U.S. economic output and labor productivity, heightening the risk of disruption across supply chains.<sup>7</sup> Increasing climate resiliency positions companies to respond to these changing and often unpredictable conditions and mitigates financial risk for investors.

### Building Competitive Teams

Social factors like diversity are also a matter of responsible businesses. Teams with diverse backgrounds and perspectives are more adept at identifying pitfalls and challenges from various angles.<sup>8</sup> Diversity creates well-rounded strategies and more effective risk mitigation approaches, which enhance a company's capacity to navigate complexities, economic uncertainties, and market fluctuations while capitalizing on opportunities.<sup>9</sup> Companies with a high percentage of BIPOC managers perform better across various sectors.

### Upholding Ethical Standards

Responsible governance is a regulatory necessity and essential strategy to uphold ethical standards and secure investor trust. Irresponsible governance creates exposure to negative consequences for proxy voting and asset manager policies, conceal risks and opportunities that are not immediately evident in traditional financial metrics, and limits stakeholders' ability to make informed investment decisions. This lack of transparency hinders market access for companies, as stakeholders may face difficulties in accurately assessing the true financial health of these businesses.

**For additional information, read the full Case for Responsible Business and Investing Practices [here](#), and find a list of key resources [here](#).**

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<sup>6</sup> USGCRP, 2023: Fifth National Climate Assessment. Crimmins, A.R., C.W. Avery, D.R. Easterling, K.E. Kunkel, B.C. Stewart, and T.K. Maycock, Eds. (November 2023, Revised February 29, 2024) U.S. Global Change Research Program, Washington, DC, USA. <https://doi.org/10.7930/NCA5.2023.CH1>

<sup>7</sup> Ibid.

<sup>8</sup> Diversity matters even more: The case for holistic impact (2023, December 5). McKinsey. <https://www.mckinsey.com/featured-insights/diversity-and-inclusion/diversity-matters-even-more-the-case-for-holistic-impact>

<sup>9</sup> The state of diversity in global private markets: 2022 (2022). McKinsey. <https://www.mckinsey.com/industries/private-equity-and-principal-investors/our-insights/the-state-of-diversity-in-global-private-markets-2022>