TIIP THE INVESTMENT INTEGRATION PROJECT

Systemic Stewardship: Investing to Address Income Inequality

Practical steps for investors redirecting financial strategies to address the systemic risk of income inequality

The second of two publications for investors addressing income inequality

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Disclosures

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Introductory letter

Leading investment groups continue to impel investors toward a system-level approach to sustainability assessment. Financial industry regulators, for example, have issued guidance for investors to address systematic risks. The Financial Reporting Council's UK Stewardship Code 2020, which went into effect January 1, 2020, directs investors to "identify and respond to market-wide and *systemic risks* to create long-term value… leading to sustainable benefits for the economy, the environment, and society." [emphasis added] [1]

The Principles for Responsible Investment (PRI) recently asked its investor-members to pursue what it calls "Active Ownership 2.0," stressing the importance of investors' stewardship of their assets broadly and the crucial role of collaboration among investors in that stewardship. Regarding system-level challenges, the PRI is explicit:

> Systemic issues require a deliberate focus on and prioritization of outcomes at the economy or society-wide scale. This means stewardship that is less focused on the risks and returns of individual holdings, and more on addressing systemic or 'beta' issues such as climate change and corruption. It means prioritizing the long-term, absolute returns for universal owners, including real-term financial and welfare outcomes for beneficiaries more broadly.[2]

While adoption of PRI's Active Ownership 2.0 concept is still in early days, there is growing evidence that major institutional investors are increasingly adopting a systemic focus when it comes to stewardship of their assets. In May 2016, for example, the International Corporate Governance Network (ICGN), which represents asset owners and managers from 39 countries with total assets of some $59 trillion, promulgated its Global Stewardship Principles, which call on its members to "build awareness of long-term systemic threats." Similarly, The Church of England Pensions Board developed a Stewardship Implementation framework that sets forth its strategies for "systemic or strategic interventions that will have a wider impact than standard corporate engagement."[3]

Active stewardship with a system-level lens protects and enhances the value of investors' assets by encouraging social and environmental practices that support sustainable financial performance. It acknowledges an investor's obligations to consider financial implications together with impact implications, thereby transcending today's market-based, "buy/sell" discipline.[4] Making this connection is an important characteristic of a system-level approach.

This type of stewardship can have true impact. When several dams of the Brazilian mining company Vale burst in the span of a few years, destroying nearby towns and killing over 250 workers and residents, the Pensions Board, which owns stock in Vale, created a coalition of investors that demanded new global safety standards in the mining industry, to be enforced by an independent body. As a result, Vale and other global mining companies agreed to undertake annual audits of their dams, implement new safety standards, and commit to public reporting. Unsafe dams have been closed and the families of victims compensated.[5]

The Church of England Pensions Board has also focused on the systemic risks of climate change, creating an "open access" climate benchmarking tool to assess the preparedness of top publicly listed companies for a low carbon economy and taking a leadership role in investor coalitions, including the Institutional Investors Group on Climate Change (IIGCC) and Climate Action 100+.[6]

Like climate change, a widely recognized systemic issue, income inequality slows economic growth, limits upward mobility, and exacerbates political polarization—threatening investments in all asset classes.[7] Also similar to climate change, mitigating income inequality requires tools and techniques that operate at a system level.

92%

of respondents said they are looking to change their stewardship approach in the next five years

Investors of all types are evaluating and adjusting the way they engage in stewardship. In a recent report conducted by Accenture Asset Management, 92% of respondents said they are looking to change their stewardship approach in the next five years.[8] The motivating factors for this change are many, but largely revolve around four key areas: value generation, increased demand for investor transparency and hands-on fiduciary duty, and a greater overall market focus on environmental, social, and governance considerations.[9]

This is where this guide enters; it shows investors how to address the system-level challenges now posed by income inequality by taking what TIIP calls a broadly conceived "systemic stewardship" approach. Systemic stewardship expands on a traditional view of stewardship as the safe-guarding and nurturing of assets. It adds to this concept investors' intentional commitments to preserve and enhance the fundamental social and environmental systems that underpin the wealth-creating potential of these assets. It acknowledges investors' obligations to manage the financial worth of their portfolios but also calls on them to mitigate risks to underlying systems as well.

In taking this approach, it considers, for example, the ability of specific asset classes to mitigate systemic risks and create systemic social and environmental benefits. It also leverages advanced techniques that help investors to, for instance, call attention to public policy debates about governmental rules and regulations that can positively or negatively impact their exposure to risks at environmental, social, and financial system levels. To do so, though, investors must acquire new tools and adopt new practices to address systemic risks and capture rewards at a system level. This form of stewardship benefits all investors not through short-term wealth extraction at the expense of systems, but through intentional investments that protect all investors' long-term wealth-creating potential.

Informed by data and case studies, investors reading this guide will learn to chart their own course for broad impact and monitor their progress as they go. This guide complements "Confronting Income Inequality: Practical guidance for how investors can address income inequality through action on labor relations, worker's rights, and financial and political equity" (2021), "Addressing systemic social risk: A roadmap for financial system action" (2020), "Why and How Investors Can Respond to Income Inequality" (2018), and the ongoing Industry Needs Assessment project. The guide also draws from the book "21st Century Investing: Redirecting financial strategies to drive systems change" (Berrett-Koehler, 2021), which shows investors what it means to manage system-level risks and rewards, why it is imperative to do so now, and how to integrate this new way of thinking into their current practice. Together, these tools make a seemingly daunting task both understandable and practical.

We hope you find this guide to be a valuable resource, and we look forward to accompanying you on the system-level investing journey that lies ahead.

William Burckart
President and COO
The Investment Integration Project (TIIP)

Executive summary

System-level investing helps investors–institutions, families, or individuals–to recognize the scope and scale of their impact and influence on environmental, social, and financial systems and guides them in intentionally managing this impact toward the goals of:

- Minimizing long-term systemic risks;
- Capitalizing on related opportunities for long-term value creation; and
- Building resilient systems that support investments across all asset classes.

System-level investing is essential to solving complex global issues that have economic, financial, social, and political consequences. By taking a narrow or short-sighted approach, traditional investment approaches and beliefs have contributed to the very global crises and inequities that threaten long-term returns.

Of all the system-level challenges confronting the world today, income inequality is one of the most pressing. With that said, this guide acknowledges the importance of wealth inequality around the world, even as its focus emphasizes income inequality. Across most regions, countries, and continents, the divide between the extremely wealthy and the working class is substantial and growing. Similar to climate change and the COVID-19 pandemic, income inequality can disrupt investors' opportunities and returns across all asset classes. Further, it can lead to political polarization, slowed economic growth, decreased social mobility, and disrupted social cohesion. In the end, all of this destabilizes systems, whether social or financial, that investors fundamentally rely on for returns.

In the U.S., wages grew

6X

faster for the top 1% between 1979 and 2019 than for the bottom 90%

Income inequality does not go away by simply waiting until it gets better. Left unchecked over the last 40 years, it has only intensified in scope and scale worldwide. Between 1980 and 2016, the incomes of the world's richest 1% of people grew twice as much as that of the poorest 50% of people.[10] Today, the world's richest 1% have more than twice as much wealth as nearly 90% of the people in the world combined.[11] In the U.S., wages grew six times faster for the top 1% between 1979 and 2019 than for the bottom 90%. But this is not a uniquely American problem; the share of the national income by the top 10% of earners in 2016 was 37% across Europe, 46% in China, and around 55% in sub-Saharan Africa, Brazil, and India.[12] In 2020, the COVID-19 pandemic exposed the presence and perils of these dramatic gaps and required significant government stimulus to forestall an even greater catastrophe.

While there are many leading social and economic indicators by which to assess income inequality, the decline of labor and workers' rights, booming CEO-to-average-worker pay ratio, and corporate tax avoidance, evasion, and competition are all driving forces and highly symbolic of the issue today. As union membership and workers' bargaining protections have declined, real disposable incomes have fallen since 2005 for one in four individuals in six of the G-7 countries.[13] In 2018, the ratio of CEO pay to that of the average worker was greater by a factor of 265 in the United States, 229 in India, 201 in the United Kingdom, 180 in South Africa, 171 in the Netherlands, and 152 in Switzerland.[14] Comparatively, in 1950 in the U.S., the average CEO made only 20 times more than their average worker.[15]

Today, 50% of the profits earned by multinational corporations abroad are booked in low-tax countries such as Ireland and Bermuda—allowing companies to substantially underpay their taxes and directly extract money from workers and the broader public domain.[16]

Black Americans earn

73.4¢

for every dollar their white peers earn

These practices enrich shareholders and executives while taking resources away from workers and other disproportionately marginalized groups–particularly women and racial and ethnic minorities. At every educational level, women earn less than men; women around the world also spend a cumulative 12.5 billion hours each day doing unpaid care work.[17] Black Americans earn 73.4 cents for every dollar their white peers earn; in Europe, Parliament introduced resolutions acknowledging structural racism as a problem in society.[18] As a result of discriminatory practices, racial and ethnic minorities experience barriers to homeownership, wealth accumulation, and education, as well as prejudicial treatment in the justice system. It's not just the decline in workers' pay and rights that affects women and racial and ethnic minorities; corporate tax schemes reduce tax revenues and therefore the funding for social programs designed to address inequities themselves.

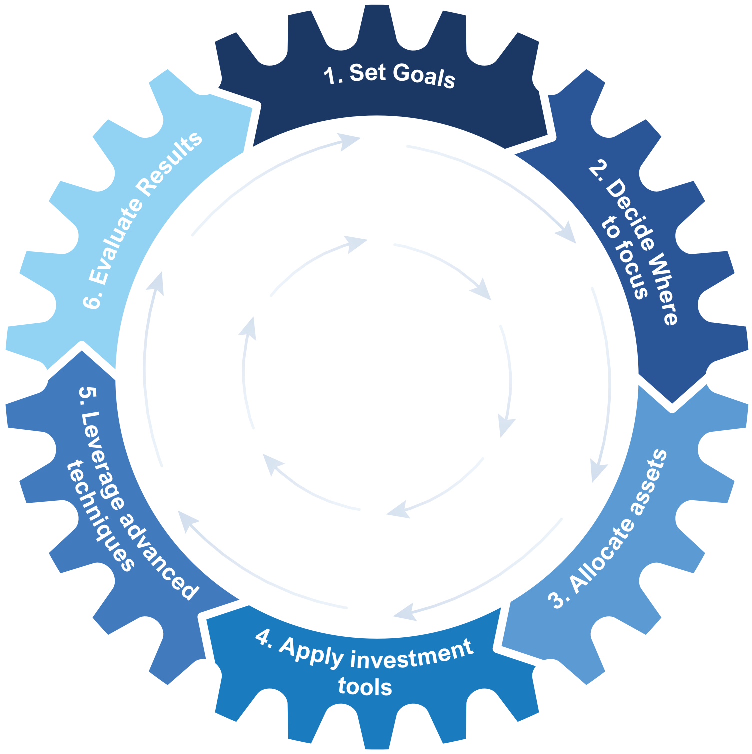
This dramatic inequality subjects society, and investors, to a dramatic systemic risk—one that affects all investments across all assets classes. However, solutions are available; while governments play a fundamental role in addressing income inequality, investors maintain a unique ability to leverage their capital and influence as an integral part of the response.

This guide acknowledges a variety of challenges that investors of all types face while exercising systemic stewardship, which expands on a traditional view of stewardship as the safe-guarding and nurturing of assets. It adds to this concept investors' intentional commitments to preserve and enhance the fundamental social and environmental systems that underpin the wealth-creating potential of these assets. It acknowledges investors' obligations to manage the financial worth of their portfolios but also calls on them to mitigate risks to underlying systems as well.

In taking this approach, it transcends today's market-based, "buy/sell" discipline and considers, for example, the ability of specific asset classes to mitigate systemic risks and create systemic social and environmental benefits. It also leverages advanced techniques that help investors to, for instance, call attention to public policy debates about governmental rules and regulations that can positively or negatively impact their exposure to risks at environmental, social, and financial system levels. To do so, though, investors must acquire new tools and adopt new practices to address systemic risks and capture rewards at a system level. This form of stewardship benefits all investors not through short-term wealth extraction at the expense of systems, but through intentional investments that protect all investors' long-term wealth creating potential.

The approaches ultimately taken by asset owners, asset managers, and those in the public and private markets will differ in certain regards. All, however, have the same underlying concern: how to protect and enhance the long-term value of their assets while acting as stewards for underlying social and environmental systems. Building on a range of conventional and advanced techniques currently at their disposal, different types of investors can draw on this guide's comprehensive, step-by-step processes for addressing system-level issues, using income inequality as a proxy. Investors will learn how to modify conventional investment tools and utilize new and advanced techniques to address income inequality by taking action on labor and workers' rights, new and advanced CEO compensation, and taxes.

Figure 1: System-level investing steps



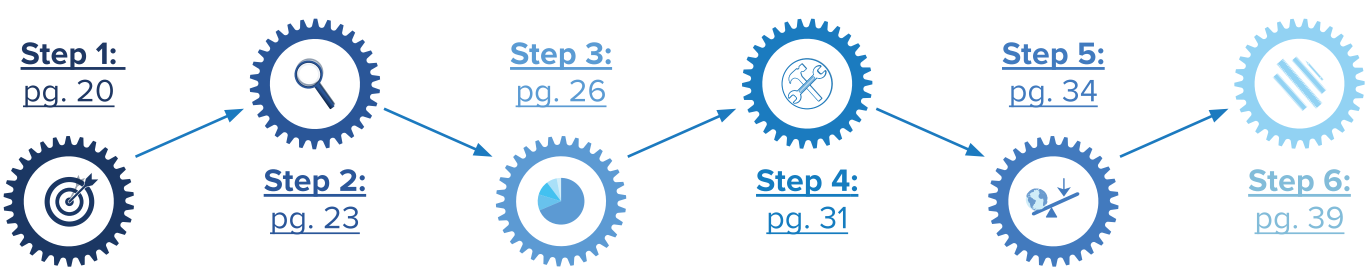
The first step in an investor's decision to integrate systemic considerations into the investment process is setting a system-level goal that affects their investments across all asset classes. Beyond building efficient portfolios and addressing social and environmental challenges as conventional and sustainable investors have done for many years, those choosing to take a system-level approach will seek to influence the social and environmental systems themselves in ways that can generate positive impacts from the outset—benefitting all investors' returns in the long run.

Next, investors must decide where to focus and commit to addressing a certain systemic issue. In addition to incorporating risk, return, and systemic challenges into their decision-making process, this guide offers system-level investors four additional criteria to consider when determining where to focus. These include the level of consensus on the issue, relevance to investors, potential for impact, and degree to which uncertainty can be managed by traditional risk-management approaches.

After deciding where to focus, investors must allocate their assets accordingly. This guide supports investors to consider the ability of specific asset classes to mitigate systemic risks and create systemic social and environmental benefits. Once these considerations are made, investors have two options to operate at a system-level. **First, they can extend conventional investment tools to exercise system-level influence**, such as investing in securities and portfolios that reflect their investment beliefs about healthy social and environmental systems and using those beliefs to engage with corporations and carry out due diligence on their investment managers. **Alternately, investors can leverage advanced techniques** described in this guide—tools designed specifically to manage systemic risks and rewards: field building, investment enhancement, and opportunity generation.

After investors follow these five steps, they must answer the question, so what? To do so, they take the sixth and final step: **evaluate results**. In addition to traditional reports on a portfolio's financial and ESG performance, this guide offers investors a six-part measurement framework for system-level investments related to a manager's beliefs and actions, and their effectiveness in various tasks and outcomes.

Click to visit each step: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A. What is system-level investing, and why does it matter?

System-level investing helps investors–institutions, families, or individuals–to recognize the scope and scale of their impact and influence on environmental, social, and financial systems and guides them in intentionally managing this impact toward the goals of:

- Minimizing long-term systemic risks;
- Capitalizing on related opportunities for long-term value creation; and
- Building resilient systems that support investments across all asset classes.

Investors can adopt system-level investing and pursue these goals alongside their ongoing management of portfolio risks and rewards and their pursuit of competitive returns. Doing so builds on the increasingly mainstream sustainable investing.

System-level investing is essential to solving complex global issues that have economic, financial, social, and political consequences. By taking a narrow or short-sighted approach, traditional investment methods and beliefs have contributed to the very global crises and inequities that threaten long-term returns.

For example, *conventional investors* traditionally seek to maximize security and portfolio returns either against a market benchmark or in absolute returns. In doing so, they generally do not factor in social and environmental considerations. In exceptional cases, they may seek to profit from what they view as market distortions due to an overreaction to such factors—for example buying the stock of coal and oil firms when they view them as undervalued.

Sustainable investors have a different take. They recognize the positive social and environmental impacts of specific investments and intentionally integrate such holdings into their portfolios. They seek ESG benefits along with their financial returns. They invest thoughtfully and ask portfolio companies to disclose more data or strengthen their standards.

They represent progress; but while sustainable investment helps investors to manage ESG impacts in their portfolios, it stops short of helping to manage systemic challenges. In thinking about climate change, sustainable investors may look at a portfolio of solar power companies and congratulate themselves because it is clean. However, sustainable investors may not consider how the growth in demand for solar may distort the market and create strains in the supply chain that lead to other environmental or labor impacts.

A growing class of *system-level investors* acknowledges that they have an impact, whether negative or positive, on the global social, financial, and environmental systems and that those systemic challenges impact their portfolios in return. These investors intentionally manage the risks and rewards at these levels to provide a stable, resilient foundation for investments across all their asset classes.[1]

Take the example of how various investors might choose to interact with climate change. Conventional investors may invest in oil drilling in the Arctic or mining metals in Greenland while at the same time looking for the next hot stock in the renewable energy field.

1 For more on changing legal considerations of investor duties regarding systemic societal and environmental issues, see the Legal Framework for Impact report prepared by the law firm Freshfields Bruckhaus Deringer, commissioned by the Generation Foundation, United Nations Environment Programme Finance Initiative (UNEP FI) and the Principles for Responsible Investment (PRI). The report provides an in-depth analysis of laws governing the investment sector with regards to investing for sustainability impact, covering 11 jurisdictions.

The key point relevant to this paper is that most investors will have a duty to consider pursuing impact on issues that are likely to affect their financial performance. Pursuing impact could mean a combination of asset allocation, policy engagement or stewardship. The report dedicates particular focus on the role of collective engagement as a key strategy for investors to discharge their duties. ngagement or stewardship. The report dedicates particular focus on the role of collective stewardship as a key strategy for investors to discharge their duties.

System-level investors ask not only what they can do for their portfolio, but what action will create fundamental change in the system that is currently generating growing income inequality

Sustainable investors may divest from fossil fuel companies partially (coal only) or entirely (oil, natural gas, refineries, and oil field services companies, too). They may add wind and solar power firms to their portfolios while looking for companies that market energy-efficient products (appliances and air conditioners) or have energy efficiency programs in place. By contrast, system-level investors look to build a portfolio of companies devoted to solar energy, wind power, battery storage, next-generation energy efficiency, sustainable forest products, and regenerative agriculture, among others, that provide a holistic vision of what an alternative world could be.

System-level investing, more broadly speaking, includes the adoption of new techniques that are explicitly designed to help investors influence social and financial systems and limit broadly occurring undesirable outcomes from the outset. Particularly forward-looking investors have pioneered a wide range of such tools designed to contend with contemporary social and financial system challenges. These tools stress collaborative action, building shared knowledge bases, setting industry standards, and creating a rising tide of investment opportunities for all investors. They focus on key leverage points that can strengthen overall social and financial systems, enhance their resilience, and ensure their long-term sustainability.

System-level issues include climate change, human rights, health systems, and income inequality, among others. Part C of this guide introduces four criteria for assessing whether an issue qualifies as a system-level issue for investment purposes. These include the level of consensus on the issue, relevance to investors, potential for impact, and degree to which uncertainty can be managed by traditional risk-management approaches. This guide uses one systemic issue—income inequality—to illustrate the six-step process investors can use to integrate systemic considerations into the investment process.

Applying a system-level lens to address income inequality

Income inequality, described in detail in Part B, is difficult for conventional investors to confront because they benefit from it themselves. They benefit when companies cut labor costs and legally avoid paying taxes, and they benefit from higher returns in the private market than they receive with government bonds.

Sustainable investors see an opportunity to balance their interests and use their influence to benefit marginalized populations. So, they ask a large company they've invested in to increase its minimum wage. They add bonds supporting low-income housing to their fixed income portfolios. They vote against a company's board that lacks diversity.

As previously described, system-level investors ask not only what they can do for their portfolio, but what action will create fundamental change in the system that is currently generating growing income inequality. So, they advocate for such things as a living wage not just by one firm, but whole industries and localities—regional, state, or national. They set their sights on new standards for corporate behavior when it comes to such issues as diversity, workers' rights, taxes, and safety, and demand that government enforce the laws and regulations already on the books in these areas. They recognize that to make system-level change happen, one voice alone is not enough. System-level investors join with their peers to amplify their message on the importance of addressing income inequality and increase their influence.

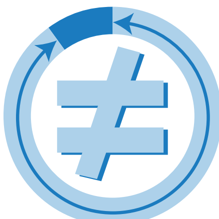
What follows is a brief on the complex issue of income inequality, including its origins, indicators, and trends of particular relevance to investors, and consequences for marginalized populations.

B. What is income inequality, and why should investors care about it?

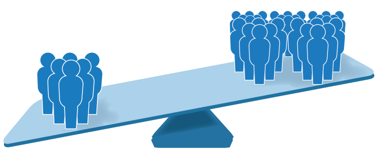
1. Introduction

Income inequality—the gap in income between the very affluent and the rest of society—is a substantial systemic social challenge within most countries and across the globe.[19] It is also a substantial contributor to wealth inequality; *the world's richest 1% of people have more than twice as much wealth as nearly 90% of people (6.9 billion) combined.*[20] Income inequality has been rising steadily for decades in many countries. In the U.S., wages grew by 160.3% for the top 1% of earners between 1979 and 2019, versus by just 26% for the bottom 90% of earners. During that same time, those in the top 0.1% experienced wage growth of 345.2%.[21]

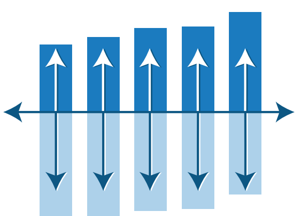
Figure 2. Income inequality by the numbers



Over the past 30 years, more than half of countries and nearly 90% of "advanced" economies have seen an increase in income inequality.



Between 1980 and 2016, the incomes of the world's richest 1% of people grew twice as much as the poorest 50% of people.



As of 2016, the share of total national income accounted for by the nation's top 10% of earners was 37% in Europe, 41% in China, 46% in Russia, 47% in the U.S. and Canada, and around 55% in sub-Saharan Africa, Brazil, and India.

On average, people in the European Union (E.U.) have income that is 11 times higher, and people in North America have income that is 16 times higher, than people in sub-Saharan Africa. Workers in countries in the northern hemisphere generally earn substantially higher incomes than their southern counterparts, with 28 of the 30 countries with the highest income per capita falling in the northern hemisphere.

2. Scope and scale of the problem

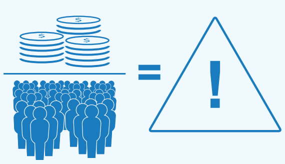
It is reasonable to expect some income inequality in any society based on differences in occupation, position, education level, and age. This type of income inequality is influenced in part by advances in technology and globalization—both of which affect the availability of jobs—as well as social policies that limit or promote economic mobility.

The extreme degree of global income inequality today, however, is accelerated by an interconnected set of beliefs and behaviors initiated by policymakers and often perpetuated by investors—whether they realize it or not.

Since the 1980s, governments, financial systems, and societies have put their faith in capital markets to generate wealth while naturally addressing systemic social and environmental challenges. They have been guided by the belief that unfettered markets can achieve the best economic outcomes, manage societal and environmental risks, and should not be obstructed by public policy and regulation.[22] As stock prices came to be regarded as a company's true value, companies doubled down on value-extracting behaviors that limited prosperity to the few at the top. A full discussion of systemic risks in the capital markets cannot occur without talking about the concentration of power that has occurred in the last few decades globally, but particularly in the West. Whether via asset managers or direct capital flows, capital maintains a unique control over labor. At the moment, the regulation and balance of these powers have been manipulated by lobbying; this power imbalance must be addressed alongside investors' decisions to truly right the ship.

These self-reinforcing corporate behaviors are partially responsible for rising income inequality. As corporations enrich investors and executives, avoid paying taxes, and underinvest in their workforces, labor standards and worker protections deteriorate; income inequality gaps widen; and the cycle repeats. As such, while there are many leading social and economic indicators by which to assess income inequality, the decline of labor and workers' rights, booming CEO-to-average-worker pay ratio, and corporate tax avoidance, evasion, and competition are all driving forces of the issue today.

Figure 3. Short-sighted actions with long-term systemic impact on income inequality



- Cutting labor costs and workers' rights decreases productivity and introduces legal, reputational, and financial risks. As income inequality widens, the middle class is hollowed out, leading to less consumption and investment.
- Funneling money away from workers to be given to shareholders leaves a company's workforce less prepared for shocks and more likely to need public support when a crisis strikes.[23]
- Dwindling workers' rights lead to the consolidation of political, social, and economic power with the few, exacerbating distrust and encouraging populism.[24]

- Disproportionate CEO compensation based on short-term profit generation reduces the buying power of the middle- and lower-socioeconomic classes—the drivers of the economy in the long run.
- Wide pay gaps between CEOs and other employees are associated with higher employee turnover, which can adversely affect a company's performance and thereby shareowner interests.[25]

- Avoiding or otherwise underpaying taxes presents risk material to a company's viability. These tax minimization strategies present significant legal, regulatory and reputational risks.[26]
- An overemphasis on tax minimization may result in poor decision making by boards.[27]
- Tax avoidance undermines government investment in public goods (infrastructure, education, and health), which support economic growth and stability.[28]

Labor and workers' rights

For generations, workers' rights have been under relentless attack in corporate management's pursuit of higher profits, cheaper labor, faster production, expanded manufacturing, and larger executive salaries. This persistent drive to minimize costs and maximize shareholder returns has affected workers' pay and conditions.[29] Labor standards have eroded, unions have started to disappear, workers have become increasingly disenfranchised, and pervasive and structural economic, racial, and gender inequality have increased worldwide.[30]

U.S. worker pay has risen just 12%, on average, since 1978. Executive compensation increased

940%

during the same period

Wages have stagnated for many in advanced economies; real disposable incomes have fallen since 2005 for one in four individuals living in six of the G-7 economies.[31] In the U.S., the federal minimum wage has been $2.13 for tipped workers and $7.25 for non-tipped workers since 2009 and should be much higher today if adjusted for inflation.[32] In fact, U.S. worker pay has risen just 12%, on average, since 1978. Executive compensation increased 940% during the same period.[33]

Today, wage stagnation for workers continues to exacerbate income inequality. The top 10% of earners receives nearly half of total global pay, while the lowest-paid half of workers receives just 6.4%."[34] Cut another way, the lowest 20% of earners—around 650 million people—earn less than 1% of global pay.[35]

Poorer countries tend to have higher levels of pay inequality, something that intensifies the hardships of vulnerable populations. In Sub-Saharan Africa, the bottom half of workers earns only 3.3% of total income. In the E.U., the same group earns 22.9% of total income.[36]

Wage stagnation is not random. It is a direct result of corporate and government policies that limit workers' bargaining power and incentivize dramatic shifts in the location and composition of the workforce.[37]

Wage stagnation for the sake of shareholder benefit introduces material regulatory, reputational, operational, and financial risk to corporations.[38] According to the Value Reporting Foundation's SASB Standards, human capital management addresses these risks in a company's operations and supply chain.[2] One criterion of evaluating human capital management, and bolstering it, is through labor practices, which include fair wages, benefits, and protections for employees.[39] As companies depress wages, they expose themselves to greater instability and uncertainty; the combination of these two can necessitate support from public institutions during times of crisis, leaving companies' operations more vulnerable.

This stagnation coincides with the diminishing collective voice and power maintained by workers. For instance, collective wage bargaining—often via unions—has declined in both the G-7 and the OECD, putting employees in a weaker position to negotiate wage increases. Across OECD countries, union membership has dropped from 30% in 1985 to just 16% in 2019, and the share of American workers in unions has plummeted to just 10% overall (6.2% for private sector workers).[40] While other countries utilize different structures to protect workers (i.e., workers' councils in Germany) these too have recently diminished in influence. For example, in Germany only 9% of the operations in the western part of the country with workers' council capacity have elected a works council; this number has remained so persistently low since the early 1990s that the government has introduced a bill to make the programs easier to start and join.[41]

2 The Value Reporting Foundation's SASB Standards identify the subset of ESG issues most relevant to financial performance in each industry.

Declining unionization, workers' councils, and other forms of workers' advocacy excludes workers from political participation in electing government officials and further consolidates political, social, and economic power with a few companies and people at the top.[42] Moreover, unionization is nearly non-existent among "non-standard" or "atypical" workers—like those that work for third party subcontractors (fissuring) and "gig economy" workers.

For instance, it would cost $2.2 billion a year to increase the wages of all 2.5 million Vietnamese garment workers to a living wage. This is about a third of the amount paid out to shareholders by the top five companies in the garment sector in 2016.[43] Without the right to organize, workers are left with little power or voice to counter the interests of shareholders and corporate executives.

Collective bargaining and unionization are not the only company decisions harming workers. Most large companies avoid taxes, depress wages, and fail to invest in innovation. They focus on cash dividends and stock buybacks, which enrich shareholders and manipulate stock prices. As William Lazonick, Phillip Moss, and Joshua Weitz explain, "Rather than do buybacks…these companies could have been persistently allocating the majority of their profits to rewarding their employees and investing in their capabilities to generate innovative products."[44] An investment in their workforce is not unwarranted. Worker productivity for many years has far outpaced wage growth; in the U.S. between 1979 and 2018, net productivity increased 69.6% while hourly pay grew by just 11.6%. Today, Americans are more productive than ever but are not paid accordingly.[45]

In the U.S. between 1979 and 2018, net productivity increased 69.6% while hourly pay grew by just

11.6%

Coinciding with global trends of offshoring work, companies are increasingly embracing fissuring and globalization and subcontracting various business functions to shift costs, responsibility for working conditions, and other liabilities to third parties (e.g., labor brokers or temporary employment agencies) to funnel greater profits back to shareholders.[46] While such actions have led to cheaper labor, quicker supply chains, and more production, they have negative impacts as well. As of 2016, 40.3 million people worldwide were subject to modern slavery.[47] Workers must also increasingly contend with unsafe working conditions. In 2014, 2.78 million people died from occupational accidents and work-related illnesses across the globe—approximately 7,500 people each day.[48] One study from California found that 87% of COVID-19 deaths in the first 10 months of the pandemic were attributed to low-wage essential workers.[49]

CEO compensation

While workers' wages have stagnated, CEO compensation has soared in recent years. This "boom" is counter to the type of growth seen in the three decades after World War II when workers and stockholders shared more equitably in the nation's prosperity, particularly in the Global North.[50] In recent decades, as a bonus for minimizing costs and maximizing shareholder returns, CEOs and other executives have seen their incomes and overall compensation packages skyrocket to astronomical levels not seen since the Gilded Age in places like America.[51] Most of the gain for CEOs came from redistributing wages from the bottom 90% to the top 1%.[52]

CEO compensation has increased steadily over the past three decades and surged in 2018 and 2019, putting it far out of pace with even the top 0.1% of wage earners, let alone typical workers.[53] Between 1978 and 2019, according to The Economic Policy Institute, CEO compensation, adjusted for inflation, rose 1,167%—much higher than the top 0.1% of wage earners, whose pay grew 337% between 1978 and 2018 (the most recent year available).

Meanwhile, the typical workers compensation grew by 13.7% over the past four decades (using figures that primarily rely on Bureau of Labor Statistics data for wages of a full-time worker in each industry).[54]

In total, CEOs of the 350 largest U.S. companies earned an average of $21.3 million in realized compensation in 2019, setting the ratio of CEO-to-worker pay at 320-to-1, up from 293-to-1 in 2018 and more than five times as high as the 61-to-1 ratio in 1989.[55] This ratio was as low as 20-to-1 in 1965.[56] In fact, the U.S. maintained the highest gap between CEO and worker pay of any nation in 2018.[57] As of that year, CEO to average worker pay was greater by a factor of: 265 in the United States, 229 in India, 201 in the U.K., 180 in South Africa, 171 in the Netherlands, and 152 in Switzerland.[58]

As of 2018, CEO to average worker pay was greater by a factor of:

265	**U.S.**
229	**INDIA**
201	**U.K.**
180	**S. AFRICA**
171	**NETHERLANDS**
152	**SWITZERLAND**

Counter to conventional thinking, the shift in CEO compensation is not related to a sudden surge in overall economic productivity; in fact, the recent rise in compensation comes at the same time that productivity has slowed.[59] Instead, the appearance of improved corporate performance used to justify increased CEO compensation reflects the growth of economic rents in CEO compensation. Further, CEO pay packages have shifted to maintain, among other things, an over-reliance on short-term measures of stock price performance and shorter vesting periods for stock awards, placing short-term value creation at odds with long-term shareholder returns.[60]

Taxes

Tax avoidance, evasion, and competition work hand-in-hand with value-extracting behaviors that enrich CEOs, harm workers, and increase income inequality. The tax issue is two-pronged; corporations, in tandem with the wealthy, have lobbied policymakers to slash income, capital, corporate, and estate taxes to some of the lowest levels in decades. At the same time, corporations commonly avoid as much tax payment as possible, even if it means engaging in tax profit shifting from one country to another.

As a result of lobbying, today, capital is taxed at a lower rate than labor. As such, the people who depend on labor for income (generally the working class) are subject to a higher tax rate than people who have capital income (generally the wealthy).[61] Prior to 1986, when the U.S. tax rate on capital gains and ordinary income was higher, capital gains accounted for 2.2% of national income each year, with an average rate of 30.9% between 1970-1985.[62] Since the 1986 tax cuts, that figure has nearly doubled to 4.1% and the top capital gains tax rests at 20% today.[63] This “explosive cocktail” of tax-free capital income undermines America’s system of taxation and threatens the sustainability of democracy and the global market economy.[64] However, the Biden administration is proposing an increase to a top capital gains tax of 39.5%.[65]

Diminishing tax rates is not a uniquely American phenomenon. The U.K. similarly reduced capital gains taxes in the 1980s, effectively "allowing private equity executives to pay a lower tax rate on their multi-million-pound bonuses than workers pay on annual wages over £50,000."[66]

These actions have direct consequences for citizens and society. Lower overall tax rates for the wealthy contribute to a growing crisis of government "going broke"–essentially generating similar or declining revenue while needing to spend more on their citizens and general public programs.[67]

U.S. total tax revenues at all levels of government shrank from about 32% of national income in 1999 to about 28% today. This decline is unique in modern history among wealthy nations. Over the past 37 years, tax revenues in OECD countries have risen from 30% to 34% of GDP while spending across OECD governments has risen from 36% to 44%, "leading to a significant buildup of public debt in many countries."[68]

Scope and scale of tax evasion by wealthy individuals

In 1980, the wealthiest Americans paid 50% of their income to taxes. Today, billionaires pay less than blue collar workers, public servants, retirees, and their own administrative staff. Due to recent cuts to estate and corporate taxes, the 400 richest Americans pay a lower overall tax rate than any other group in the country. Alongside tax evasion, the pool of money controlled by wealthy individuals is becoming larger, increasing the aggregate amount subject to tax evasion practices. In 2020 alone, the world's wealthiest 500 people saw their fortunes increase by $1.8 trillion to reach $7.6 trillion in total.

Enhancing tax enforcement at the top of the wealth distribution can be desirable for at least three reasons:

- It has the potential to raise government revenue significantly as the wealthiest taxpayers account for a large portion of total taxes.
- It may help restore the progressiveness of the tax system, which is currently being eroded by very high evasion rates at the top.
- It may mitigate the secular rise in inequality as top income and wealth shares continue to increase in many countries.

Source: Emmanuel Saez and Gabriel Zucman, The Triumph of Injustice: How the rich dodge taxes and how to make them pay (New York: W.W. Norton & Company, 2020); Sheelah Kolhatkar,"The Ultra-Wealthy Who Argue That They Should be Paying Higher Taxes," The New Yorker, January 6, 2020, https://www.newyorker.com/magazine/2020/01/06/the-ultra-wealthy-who-argue-that-they-should-be-paying-higher-taxes; Ben Steverman and Benjamin Stupples, "The Wealth Tax Is Going Global," *Bloomberg*, January 6, 2021, https://www.bloomberg.com/news/articles/2021-01-06/tax-code-changes-wealth-taxes-considered-from-california-to-germany.; Gabriel Zucamn et al., *Tax Evasion and Avoidance*, December 28, 2019, http://gabriel-zucman.eu/files/AJZ2018b.pdf

Corporations are also paying less and less as a result of sophisticated tax avoidance schemes, further entrenching the power imbalances that perpetuate income inequality. Historically, America's share of national income paid by corporate tax revenue was 4-5%; today, it barely exceeds 1%.[69] In the U.K., more than 50% of the subsidiaries of foreign multinational companies currently report no taxable profits.[70] In the U.S., 55 of the largest corporations, most on the Fortune 500 index, paid no federal corporate income taxes on $40 billion of profits in 2020. These companies include Nike, FedEx, Salesforce, Dish Network, HP, and other household names.[71] The Government Accountability Office estimates that the U.S. loses $458 billion in revenue each year from tax avoidance and evasion.[72]

How are they doing it? Two common tactics solidify tax avoidance into company practice. The first is tax competition, a practice wherein countries or other localities offer lower tax rates to entice investment and operations by multinational corporations. Tax competition can occur for both individuals and corporations, although it is more common for the latter. It leads to self-reinforcing outcomes. Countries continually bid for companies to book their profits in their jurisdiction by lowering their tax rates, thus leading other countries to lower their tax rates in turn to compete.[73] As a result of rising global tax competition, the average corporate tax rate worldwide has fallen from 49% in 1985 to 23% today. In the U.S., it has fallen from 50% in the 1950s to 17% today.[74] There was only one country, France, with a corporate income tax rate above 30% in 2020, compared to 23% in 2000.[75]

40%

of all multinational profits are shifted into tax havens around the world

A direct outcome of tax competition is profit shifting, the second tactic that companies use to avoid taxes. Profit shifting occurs when a multinational corporation "shifts" profits from a higher tax jurisdiction to a lower tax jurisdiction, often one with 0% or close to 0% tax rates. This practice is a relatively recent trend. In the 1970s, despite a 50% corporate tax rate, multinationals booked 95% of their foreign profits in places with high-tax rates, like Canada, the U.K., and Japan. Today, however, 40% of all multinational profits are shifted into tax havens around the world. In the U.S., 60% of multinational profits made abroad are booked in low-tax countries today (mostly Ireland and Bermuda).[76]

In fact, in 2016, U.S. multinationals booked more profits in Bermuda and Ireland than in the U.K., Japan, France, and Mexico combined.[77] That same year, U.S. companies also booked 20% of their non-U.S. profits in "stateless entities"—shell companies that are incorporated nowhere and taxed nowhere–amounting to $100 billion in profits with no tax jurisdiction.[78]

Shifting profits to a country with a lower tax rate does not result in job creation in that country – 95% of the 17 million workers employed outside the U.S. work in places with high tax rates. Fewer than 1 million people work in countries considered to be tax havens.[79]

Efforts underway to limit tax avoidance (see profit shifting and transfer pricing sidebar) could serve to intensify tax competition—particularly for real investments. Additionally, the 2017 reduction in the U.S. federal corporate income tax rate is viewed as a likely precursor to cuts in other countries.[80] However, in early 2021, the Biden administration issued a plan to raise the corporate income tax rate to 28% from 21%.[81] The administration estimates it would generate $2.5 trillion in revenue over the next 15 years, to be spent on infrastructure. The political viability of the plan remains to be seen.

In the end, while companies receive substantial tax breaks, countries are left to contend with nonexistent tax revenue.[82] Less tax revenue leads to less funding for services that companies depend on for the proper functioning of their businesses as well as critical services that benefit and uplift society. As tax bases diminish, social, environmental, and financial systems deteriorate.[83]

A note on profit shifting and transfer pricing

Among the many techniques employed to dodge taxes, profit shifting and transfer pricing are particularly widespread. Profit shifting occurs when a multinational corporation "shifts" profits from a higher tax jurisdiction to a lower tax jurisdiction, often one with 0% or close to 0% tax rates.

For instance, many corporations use letter box companies in the Netherlands to avoid taxes. At the same time, the Netherlands is facilitating corporate tax avoidance through bilateral tax deals. For example, a tax agreement between the Netherlands and Uganda gives Dutch subsidiaries of the French oil multinational Total and its partner CNOOC special tax advantages. Oxfam estimates that, "unless renegotiated, the treaty could allow the companies to avoid an estimated €245 million ($287 million) in tax in Uganda over a 25-year period. Loss of tax revenues will reduce the funding available for public services such as healthcare in a country which has one of the highest maternal mortality rates in the world."

Transfer pricing, a strategy and system allowing companies to determine the price of a transaction between entities under common ownership or control, remains common in today's interconnected world as well. To address this issue, the G-20/OECD project on Base Erosion and Profit Shifting (BEPS) has made significant inroads in international tax cooperation, but challenges remain. In particular, the arms-length principle that allows transactions between related parties to be priced as if they were between independent entities continues to allow profitable firms to pay little tax. So how does this all play out in real life? Take Google, who sold search and advertising technology to "Google Holdings" in Ireland, which pays taxes in Bermuda (a state with no corporate tax). While the sale price is not public, Google paid $241 million in taxes the year of the sale. Even if this was all from the sale of IP, that would mean the technology was sold for less than $700 million. In 2017, Google Holdings made $22.7 billion in Bermuda, but with a corporate tax rate of zero, Google paid no taxes on the earnings.

Skype offers another example. After its founding, Skype moved its IP to a subsidiary in Ireland where the corporate tax rate is a low 12.5%. This IP was sold for €25,000 and not a few months later was bought by eBay for $2.6 billion. This move allowed the sale of the IP to be taxed at a significantly lower rate than if the IP has not been sold to a subsidiary in Ireland.

Source: Emmanuel Saez and Gabriel Zucman, The Triumph of Injustice: How the rich dodge taxes and how to make them pay (New York: W.W. Norton & Company, 2020); International Monetary Fund (IMF), IMF Policy Paper: Corporate Taxation in the Global Economy, IMF, March, 2019 https://www.imf.org/en/Publications/Policy-Papers/Issues/2019/03/08/Corporate-Taxation-in-the-Global-Economy-46650.

3. Consequences of income inequality

There is an argument that a certain amount of income inequality can be good for society; it can incentivize hard work and encourage entrepreneurship. However, today's extreme income inequality does more harm than good—it slows economic growth, leads to more frequent and deeper recessions, limits upward mobility, aggravates social cohesion, and exacerbates political polarization. In particular, women and racial and ethnic minorities are disproportionately harmed.

Gender disparities

In addition to experiencing widespread wage inequality, women must contend with systemic disadvantages that hinder their financial and career growth and safety.

Despite being more likely than men to hold an advanced degree, women earn less than men at every single education level.[84] One explanation is that earnings for American mothers fall 31% on average after the birth of their first child, relative to the child's father's earnings.[85] Women's labor force participation is just 47% (compared to 74% for men), in large part because globally women and girls (especially those living in poverty and from marginalized groups) spend a cumulative 12.5 billion hours each day doing unpaid care work—work that adds at least $10.8 trillion to the economy.[86] Those women who do work outside of the home earn, on average, $0.85 for every $1.00 earned by a man and have net wealth equal to just 62% of men's (on average, across a sample of 22 OECD countries).[87] Women account for 71% of modern-day slaves.[88]

Women earn less than men at every single education level

Women make less money for the same work, have fewer rights, and are much more likely to do unpaid work than men. Therefore, they rely more on government-funded services like healthcare and education. Corporate profit shifting hurts them by reducing revenues for such support.[89] By not addressing the gender gap in work and opportunity, global GDP could lose out on $13 trillion by 2030.[90]

The pandemic has exacerbated the gender divide. Globally, employment losses experienced by women stood at 5% at the beginning of 2021, compared to 3.9% for men.[91]

Racial and ethnic discrimination

Gender is not the only contributing factor. Structural barriers ingrained in the fabric of society—spanning from education to employment, healthcare, and pay—leave certain racial, ethnic, and religious groups subject to discrimination and relegated to the bottom of income and wealth distributions.

In the U.S., for example, Black Americans face wage inequality, earning 73.4 cents for every dollar made by their white peers. Black women earn even less—only 62 cents on the dollar compared to white men.[92] Black workers are also twice as likely to be unemployed.[93]

Moreover, Black entrepreneurs in the U.S. have been denied access to loans and capital at a rate twice as high as their white counterparts, costing the U.S. as much as $13 trillion in lost revenue per year over the past 20 years.[94] Outside of employment, decades of discriminatory housing and lending policies have disproportionately prevented Black families from the wealth-generating benefits of homeownership.

Similarly, other racial and ethnic minorities face comparable barriers; in the U.S. in 2019, Hispanic homebuyers paid a significant premium to borrow money, paying 43% more to close on a home purchase and 30% more in interest compared to non-Hispanic White applicants.[95] Today, at each and every level of education, people of color are paid less than their white counterparts, have fewer assets than their white counterparts and accrue less wealth, and experience higher rates of unemployment.[96]

Black entrepreneurs in the U.S. have been denied access to loans and capital at a rate twice as high as their white counterparts, costing the U.S. as much as

$13T

in lost revenue per year over the past 20 years

Globally, racial and ethnic minorities experience barriers to economic well-being, education, political participation, and employment in most nations.[97] These inequities have micro- and macro-economic consequences. In France, GDP could jump 1.5% over 20 years by reducing racial gaps in employment.[98] Racism is estimated to have cost Australia $44.9 billion between 2001 and 2011.[99]

41%
of Black-owned businesses have permanently closed as of July 2020 versus 17% of white-owned businesses

COVID-19 has widened these existing gaps. Women, racial and ethnic minorities, and migrant laborers were more likely to get sick and die from COVID-19 or to experience the economic devastation experienced by the shutdowns. Overall, these groups are more likely to work in industries deemed essential, exposing them to the virus at greater rates, and work in occupations under short-term, atypical, or gig contracts leading to early layoffs. These same groups were also less likely to have access to sick paid leave, health insurance, or the ability to work remotely.[100]

In the United States, for example: 41% of Black-owned businesses have permanently closed as of July 2020 versus 17% of white-owned businesses, and Black Americans are 3.5 times more likely to die from COVID-19 than white Americans.[101]

Practically speaking, income inequality is not uniformly experienced across all demographics and geographies. Discrimination is magnified by social identities, such as gender and race, and individuals with different cultural and racial backgrounds will have vastly different experiences with income inequality. This paper highlights some of these inequities in order to illustrate the scale of income inequality. However, more research is needed to fully examine the breadth and depth of these issues.

Broader economic and financial consequences

Race and gender inequities further slow consumer spending and GDP growth. Lower- and middle-income earners typically spend a higher proportion of their income than higher earners, and therefore stimulate more economic growth.[102] The failure of companies and governments to keep pace with pay for typical workers results in a shrinking middle-income earning population. Because an even larger share of income is being shifted to wealthy households that save rather than spend, economic growth is suppressed.[103]

For example, when the income share of a country's wealthiest 20% of people increases by just 1%, GDP growth declines 0.08% in the subsequent five years. On the other hand, an increase in the income share of a country's poorest 20% of people is associated an increase of 0.38% in GDP over the same period.[104] On a macroeconomic level, as of 2017, rising inequality had slowed growth in aggregate demand (household, government, and business spending) by 2 to 4 percentage points of GDP annually. Josh Bivens further illustrates the severity of this effect, explaining that "to offset the hit to demand posed by rising inequality, we'd need to enact a policy each and every year that delivers a boost of the rough magnitude of the peak [American Recovery and Reinvestment Act] boost."[105]

As of 2017, rising inequality had slowed growth in aggregate demand (household, government, and business spending) by
2 to 4
percentage points of GDP annually

Other social and political consequences

Chasms between the income, wealth, and power of the highest and lowest earners affect more than buying power and aggregate demand; they have important social consequences. Extreme income inequality introduces into society social discontent and tension, political polarity and tendencies toward nationalistic populism, trade wars, and general social and political unrest, instability, and dysfunction.[106]

Income inequality arguably influenced the tenor of recent acrimonious elections in the U.K. and U.S.; has influenced the political climate in Austria, France, Hungary, the Netherlands, and Poland, among other countries; and diminished faith in government worldwide, leading to growing support for authoritarian parties and political figures.[107] Similarly, the declining presence of labor unions has led to a downturn in workers' voting participation, fundamentally changing the influence and voices workers have around how government acts on issues relevant to societal systems and workers.[108]

Moreover, systemic challenges can compound when they intersect. The threat of climate change demands immediate action. At the same time, phasing out coal and other fossil fuels threatens well-paying jobs, thereby exacerbating income inequality. Inability to deal with the prospects of income inequality in these industries paralyzes action on climate change. In this case, calls for a "just transition" are crucial to simultaneously contend with these interrelated complications.

Investors should therefore be concerned about income inequality not only in and of itself but also for its potential to complicate their ability to contend with other systemic challenges.[109] If unrest and conflict paralyze our political systems and prevent the compromises necessary for an inclusive public good, we will see underinvestment in the economy, continuing discrimination, and increased demands on a weakened government for social services that it does not have the resources to provide. The resulting weakening of social, environmental, and financial systems introduces risks to investors in the long term. As a result, income inequality has the potential to affect investor portfolios across all industries and asset classes.[3]

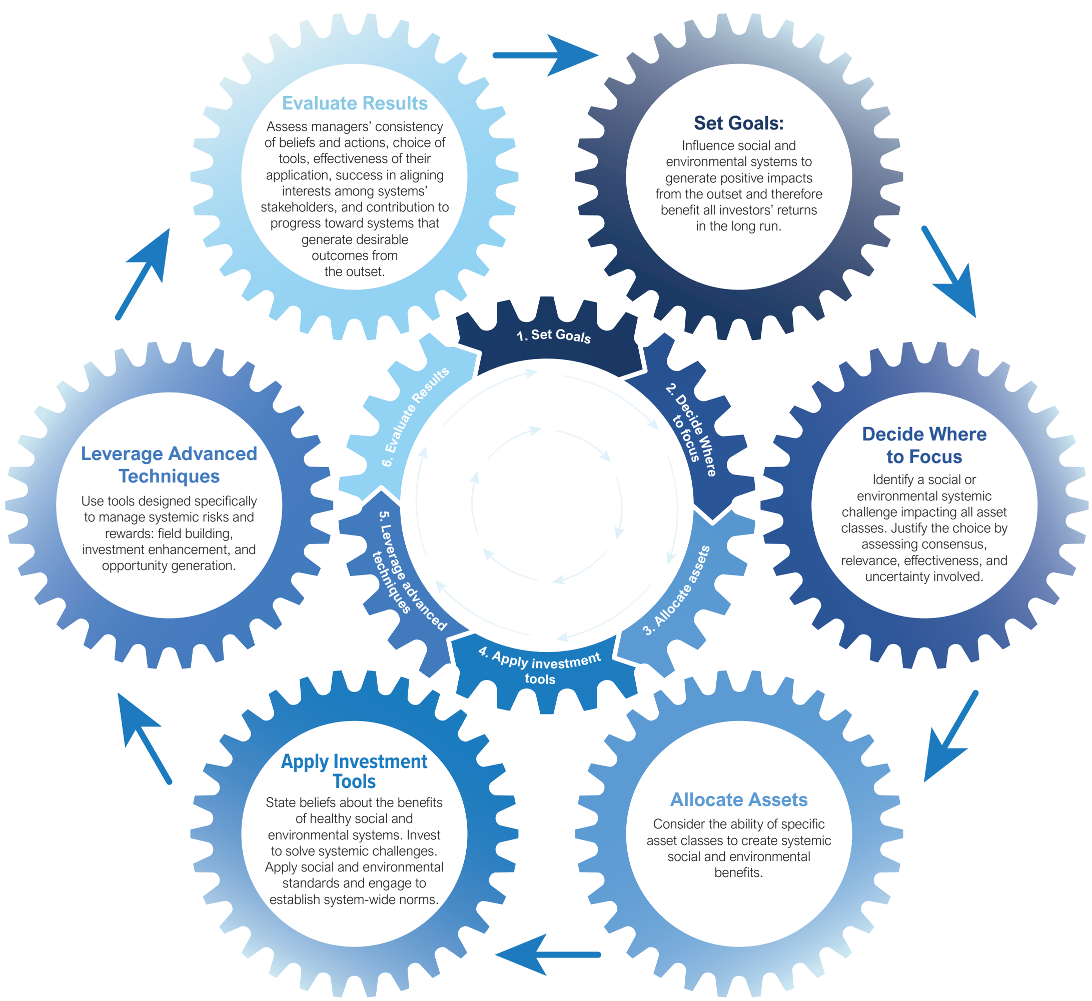
3 Income inequality meets the criterion of "relevance" used to determine if an issue is systemic because it can affect the long-term financial performance of portfolios across all asset classes.

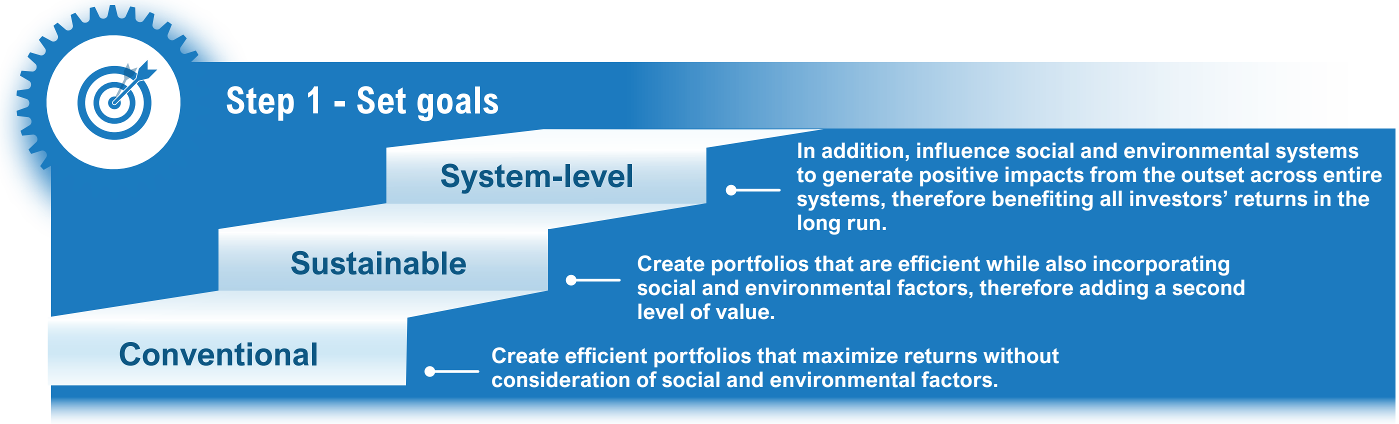
C. How can investors integrate systemic considerations into the investment process to address income inequality?

While income inequality is a persistent problem, investors can take meaningful action today. This guide helps investors to mitigate income inequality directly through the levers of labor and workers' rights, CEO compensation, and taxes—thereby indirectly addressing issues of gender, geographic, racial, and ethnic inequities. Most importantly, this guide lays out a six-step process that investors can use to address any system-level issue through an enhanced stewardship approach. Figure 1 summarizes the process for incorporating system-level investing. The journey begins with a willingness to build on and extend the best practices from conventional and sustainable investment to embrace the contexts of the social and environmental systems in which they operate.

The six key steps of the process are the same for all investors: set goals, decide where to focus, allocate assets, apply investment tools, leverage advanced techniques, and evaluate results. This guide illustrates the need for and benefits of incorporating a system-level perspective at each step in the process. This process puts a powerful tool for change in investors' hands. It requires balance, some of which is already inherent in conventional and sustainable investment: balancing risk and reward, income and asset appreciation, social benefit and financial returns, public good or harm and private gain. Such balancing acts may not be easy; that simply means that managers must sharpen and demonstrate their skills.

Figure 4: Steps in the process





The challenge

While the global climate crisis has resulted in perhaps the greatest awareness among investors of the importance of systemic issues, the costs of the pandemic and rising income inequality are quickly expanding investor understanding of potential risks and impacts associated with social issues.

The COVID-19 pandemic and its related social and economic fallout demonstrated how the drive to efficiency can leave a system—in this case, the global healthcare system, but all supply chains in reality—overly vulnerable to disruptions that can wreak havoc on others. Although finance cannot prevent the threat of the next pandemic, intentional system-level decision-making by investors can help prepare for it and mitigate its worst social and economic impacts. Although it is difficult to demonstrate the impact of a single investor or single factor on a paradigm or system, multiple actors working in tandem are more likely to bring about measurable system-level change.

Conventional investors' goals focus on maximizing returns by beating the market

The goal of conventional investors is to create efficient portfolios that maximize returns, thereby benefitting society. Derived from Modern Portfolio Theory (MPT)–a method of managing risks and rewards through diversification, market efficiency, and risk tolerance–conventional investors assume systemic risks are beyond the ability of asset owners and managers to influence, and therefore accept no responsibility for their action or inaction.

While the benefits of this philosophy are many, academics and practitioners in the investment community have also recognized its limitations: it assumes that markets operate without transaction costs, have unconstrained liquidity, have a risk-free investment option always available, and are composed of rational actors who consistently act in their own best interest. Most important, though, it assumes that "the market" has risks and rewards that affect investors that they themselves cannot influence–an incorrect assumption that the 2008 financial crisis highlighted dramatically.[4]

Today, we live in an increasingly populous and prosperous world of 7.8 billion people with worldwide wealth estimated at over $360 trillion and growing.[110] The sheer size and reliance of all modern enterprise on the financial services industry, both relative to other industries and in absolute terms, gives its collective actions potential for creating unintentional harm as well as helpful change. It is only natural that new goals beyond beating the market have emerged as well.

4 For more on the limitations of Modern Portfolio Theory (MPT) for addressing systemic risks see, Moving Beyond Modern Portfolio Theory: Investing That Matters (Routledge, 2021), written by Jon Lukomnik and James P. Hawley.

Sustainable investors' goals focus on social and environmental factors

Sustainable investors believe integrating social and environmental considerations into their investments can add value to their security selection and portfolio performance.

Sustainable investors use different frameworks to address different issues. Some use the United Nations Sustainable Development Goals (SDGs), a collection of 17 interlinked global goals designed to be a "blueprint to achieve a better and more sustainable future for all."[111] Others use the Value Reporting Foundation's SASB Standards Materiality Map, which provides a framework for determining sustainability issues by assessing and mapping the materiality impact of noteworthy ESG issues across key industry sectors. While not perfectly uniform in scope and scale, assets driven by ESG-data hit $40.5 trillion in 2020.[112] To date, groups like the Impact Management Platform—a global, sector-wide initiative —have developed a set of shared principles, standards, and benchmarks for defining, measuring, and reporting on impact, which bridges various frameworks to create more industry-wide uniformity.[113]

However, in today's practice, sustainable investors tend to confront social and environmental challenges after they have been generated by the current system. Failing to fundamentally reshape systems means problems are likely to recur.

Opportunity for action

System-level investors push themselves to achieve goals that focus on the *paradigms* that underlie systems. Paradigms are "philosophical and theoretical frameworks within which we derive theories, laws, and generalizations."[114] To change the output of a system with a reasonable degree of consistency, one often must change the paradigms that it operates under. Using one of the SDGs as an example, investing in decent work and economic growth (SDG 8) would require a goal of shifting the paradigm away from that of global reliance on cheap labor.[5]

To set goals to shift paradigms, investors must first assess the relationship between current paradigms and current systemic results. Then, investors can develop a theory for alternative paradigms and better results. For example, if the current paradigm of maximizing short-term profits is connected to unsafe working conditions and child labor, a focus instead on dignified work for all may lead to safer working conditions and full employment for adults. With a clear definition of both old and new paradigms in mind, investors can then develop with reasonable specificity goals and milestones for progress.

The promise of short-term payoffs often prevents many investors from joining in newer, less conventional endeavors with long-term benefits to a system as a whole. What investors all must recognize and acknowledge is that a long-term view—one that takes into account the health and preservation of essential systems and does not bow to short-term returns over all else—makes it easier to predict and mitigate the nature and extent of the global disruptions to come.[6]

Investors can take a few decisive steps to put better guardrails in place. These include supporting governments resilient enough and with deep enough pockets to build safeguards and kindle economic recoveries; insisting that companies understand their business models and prepare backstops to prevent their meltdown; and preparing for potential systemic breakdowns. With the right goals and tools, investors can help stabilize these systems while also making long-term, profitable returns.

5 For more on investing with alignment to the SDGs, see Beyond Alpha's, "We Need to Talk: Why It's Time for Institutional Investors to Embrace SDG-Aligned Investing."

6 A note on investors' duties in impact: Fiduciary Duty in the 21st Century established that all investors have the duty to consider ESG factors as they are material to security valuations, "Failing to consider long-term investment value drivers, which include environmental, social and governance issues, in investment practice is a failure of fiduciary duty."59 In 2020, the U.K. Financial Reporting Council issued guidelines stating the consideration of systemic risks such as climate change was appropriate in investors' role as stewards of assets.

A closer look: Cbus

Cbus is the Australian Construction and Buildings Union Superannuation Fund. Cbus's Responsible Investment Policy states its commitment not only to integrate ESG considerations into security selection and portfolio construction, but also to use its "strategic activities" to influence "the shift towards a sustainable financial system."

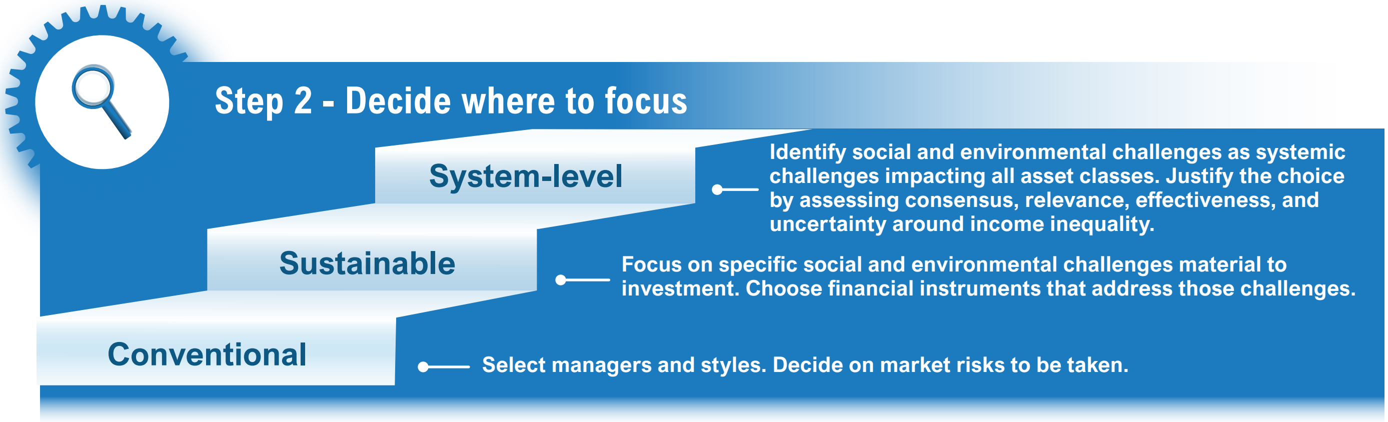
The Fund applies this approach in all of its investments across all asset classes and all investment styles. To enhance its effectiveness, the Fund actively collaborates with groups of like-minded investors to increase the influence and success of responsible investment and complex market transformation.[115]

With respect to income-inequality-related systemic concerns, Cbus reports that it has partnered with the New South Wales government to promote investments in low-income and affordable housing, leading to an initial $10 million investment. It believes that further collaborations with other state governments will enable greater institutional investment into social and affordable housing, both by providing capital to build housing and by creating and maintaining jobs in building construction.[116]

In 2019, Cbus' CEO became a member of the Australian Sustainable Finance Initiative's Steering Committee. The Initiative is a joint undertaking of financial regulators and major banks, insurance companies, and pension funds. It will make recommendations on how the Australian financial industry can best contribute to "a more sustainable and resilient economy" aligned with climate change and other sustainability goals.[117]

Table 1. ***Investors & institutions transitioning to a focus on systemic issues***

	CBUS	CalPERS	GPIF	PGGM	WSIB
Systemic Focus	Cbus formally states that it believes that "responsible investment extends to influencing the shift towards a sustainable financial system."[118]	The California Public Employees Retirement System (CalPERS) established a belief statement: "Encouraging external managers, portfolio companies, and policy makers to engage in responsible environmental practices is important to risk management. This means making wise use of scarce resources, considering impact, and addressing systemic risks, such as climate change."[119]	The Government Pension Investment Fund (GPIF) of Japan, one of the largest pension funds in the world, believes that improving the governance of the companies they invest in while simultaneously minimizing negative environmental and social risk is essential for the profitability of the portfolio in the long term.[120]	The Dutch pension fund manager PGGM has allocated a multi-billion-dollar piece of its assets into an impact- or solutions-based portfolio. This portfolio focuses on four system-level issues: climate change, food security, health care, and water.[121]	The Washington State Investment Board (WSIB) states that as a long-term investor it considers "all identifiable risks in [its] investment process and believe[s] thoughtful consideration of these evolving global challenges is inseparable from long-term investment strategy and performance."[122]



The challenge

Once system-level goals are set, investors face two main barriers when deciding on which system-level issue to pursue. First, **agreement on what qualifies as a system.** This guide offers investors four criteria for assessing if an issue rises to a system level, described in the next section. Meeting all four criteria is a very high bar, particularly factoring in the constraints on time and resources. The implication is that only a limited number of system-level considerations will be appropriate for investors at any given time; therefore, many investors are needed to solve the many problems at hand.

The second barrier is the sheer complexity of these issues. By their nature, **system-level issues are substantial, complicated, and require long-term ingenuity.** As such, after an issue meets the four criteria for being at a system level, investors must accurately match their skill set with the requirements of the problem at hand.

Income inequality is one issue where system-level investors are essential to creating meaningful and lasting change. Conventional investors find income inequality particularly difficult to confront because they are mainly concerned with the selection of managers, styles (active vs. passive), asset allocations, and the level of risk being taken; they believe they will benefit from many of the practices that drive income inequality, and therefore have no reason to invest in strategies to confront this issue.

Sustainable investors add the selection of social and environmental challenges they want to tackle as well as the financial instruments appropriate to that task. They see the harm arising from issues like income inequality and the destabilizing effects it has on society.

While there are certain system-level issues many investors agree upon, the way these issues manifest themselves can vary greatly depending on industries and sectors. System-level issues transcend industries but may not manifest themselves similarly in all industries. As such, industry- and sector-specific criteria need to be considered when deciding where to focus, along with other steps in the system-level stewardship process.

Opportunity for action

System-level investors face a related but different task from other investors in deciding where to focus. They look beyond individual portfolios to ask: How can we reduce income inequality and resulting instability in the system with investments that create a rising tide of opportunities for all?

They recognize that system-level changes require coordinated action. As such, system-level investors join with their peers to amplify messages and tactics that address income inequality and increase their influence. Together, they begin to control the systemic risks that income inequality poses and create new, and better, investment opportunities.

The first question that investors will want to resolve after deciding on the appropriateness of a system-level approach is: *On which issues within which systems should we focus?*

System-level investors factor in the complex challenges and multiple contributing factors that characterize systems at the highest social and environmental levels. While relatively simple subsystems may contribute to the larger-scale systems they are concerned with, a broad focus is necessary to reorient the overall system effectively toward desirable outcomes.

Because the potential range of system-related challenges that investors might address is substantial and because not all considerations can be justified as system-level in their scope, investors need criteria against which to assess various potential considerations. System-level issues that warrant investor consideration and attention conform to four criteria:

- **Consensus: a general agreement among authorities on the issue;**
- **Relevance to investors: the potential for the issue to affect investors' portfolios positively or negatively;**
- **Potential for investors' policies and practices to effectively impact or influence the issue at a system-level; and**
- **Uncertainty about potential outcomes caused by disruptions related to the system-level issue that cannot be addressed through traditional portfolio risk-management techniques.**

Issues that share these four criteria rise to a level of concern such that long-term investors can reasonably approach them as systemic in nature. Income inequality, the focus of this guide, qualifies as worthy of a systemic approach not only because Nobel Prize winning economists like Joseph Stieglitz and Paul Krugman and prominent members of the investment community, such as PRI and Établissement de retraite additionnelle de la fonction publique (ERAFP), validate its dangers (consensus), but because these dangers will impact investors across all asset classes (relevance), investors can have positive influence when addressing them (potential impact), and income inequality creates uncertainties so great that conventional investment techniques can't manage their risks (uncertainty about outcomes).

A closer look: The California Public Employees Retirement System

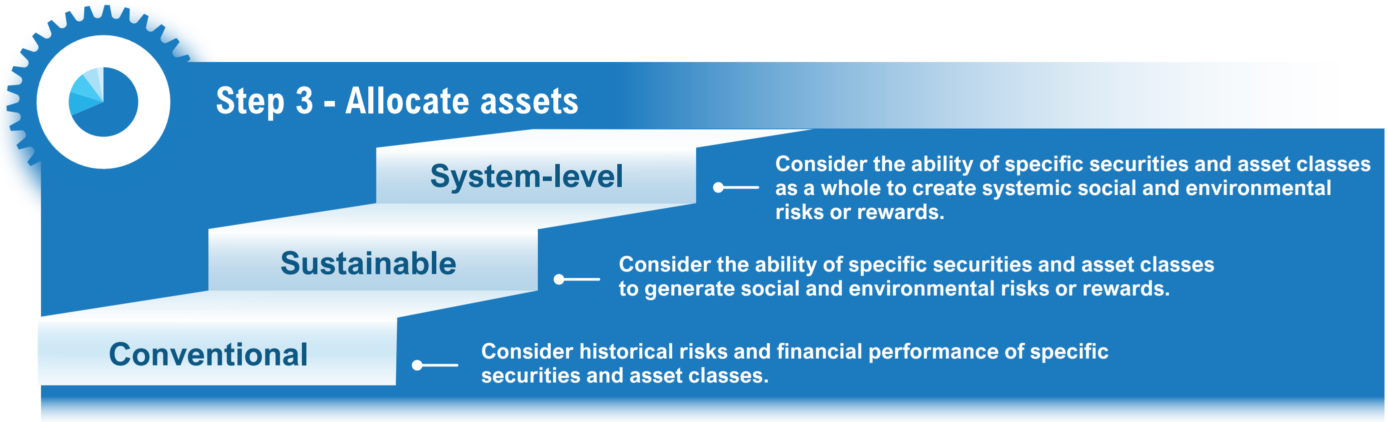
The California Public Employees' Retirement System (CalPERS), which manages $444 billion as of 2021 to provide retirement and health security for its state, school, and public agency members in California, has been at the forefront of adopting a systemic lens as one component of its management of risks and returns.

CalPERS has clearly stated its belief, for example, that three forms of capital are used to create value in the long term, therefore making them critical to "capital formation" and the overall health of their funds. These capitals include: physical capital (environmental), human capital (social), and financial capital (governance).[123] Among its human capital concerns, CalPERS includes fair labor practices, health and safety, responsible contracting, and diversity. These are among the difficult-to-value factors that CalPERS has concluded lead to the proper functioning of human capital and take investors beyond the simple price of securities.[124]

CalPERS has begun research on economic inequality, workforce compensation, workforce transition, and diversity and inclusion, along with other human capital related topics. Paired with this research are engagements with public and private companies on a variety of human capital issues identified as risks in its portfolio.[125]

Table 2. Criteria for choosing the system-level issue of income inequality

	Consensus	Relevance	Effectiveness	Uncertainty
Definition	An issue that is debated globally and upon which general agreement about its overriding importance has been achieved.	An issue with substantial potential to impact positively or negatively the long-term financial performance of not simply one portfolio, but portfolios across most asset classes.	An issue with substantial potential for investors to influence positively or negatively the functioning of a given system.	An issue with unpredictable and unquantifiable uncertainties if disrupted at a systems level.
Importance	Ensures consideration of issues that have been widely debated and that do not represent narrowly conceived, idiosyncratic interests.	Ensures consideration of issues that are broadly relevant, either positively or negatively, to the investor's long-term financial interests.	Ensures consideration of issues for which investors' decision-making can be effective in producing positive or negative impact at a systems level.	Ensures consideration of issues with substantial potential to create uncertainties and to reduce the scope of these uncertainties.
Income Inequality Examples	The issue of living wages, among others, is broadly recognized as a crucial component of healthy societal systems. Simply put, society cannot function smoothly without them.	Income inequality slows economic growth, leads to more frequent and deeper recessions, limits upward mobility, aggravates social cohesion, and exacerbates political polarization.	To mitigate current income disparity, investors can support calls for fair compensation and a living wage, both in the companies they invest in and other industries at large.	Income inequality creates issues with difficult-to-predict outcomes, such as level of diminished economic growth and stability, as well as uncertain political continuity.



The challenge

An initial step for investors is deciding how to allocate resources—financial and staff time—to the different assets in their portfolio. One of the challenges they face is understanding how these choices can bring about real change in addressing social and environmental challenges at a system level.

To do this properly, investors must determine which of the asset classes they invest in can best address income inequality. Each asset class comes with its own benefits and drawbacks: venture capital with a tendency to favor gig-economy workplace business models that can have systemically negative impacts; government agency bonds such as Fannie Mae that support low-income and affordable housing nationwide; public equities of companies that can influence basic labor standards for the largest employers in the country; municipal bonds that can support local economic development; and real estate that can influence the built environment positively or negatively. Each asset class offers its own special set of opportunities or challenges for investors to note in their asset allocation process and tailor as they view appropriate to the system-level issue on which they are focusing.

Conventional investors typically balance their desired returns with their risk tolerance, and their need for income with their prospects for market appreciation. Alignment with social and environmental goals or selection of securities with social and environmental positives in each asset class is not part of the picture.

Sustainable investors, once having decided on their asset allocation, select individual securities that are aligned with their social and environmental goals. They may also encourage companies to expand practices that can enhance their social benefits alongside their profitability.

These approaches do not get to the heart of the challenge; they don't consider how the assets specific to each class can impact the system itself, only how they function within a portfolio.

Opportunity for action

Investors large and small can think creatively about how to use asset classes to impact income inequality. The first step is to decide what asset classes to use: stocks or bonds, venture capital or real estate, private equity, and cash. Of course, a primary concern is the historical returns of these asset classes. After all, investors want their money back with a return. Some classes have returned more than others, some are quite risky, and each serves different societal functions.

System-level investors are aware of the social or environmental utility of each asset class. Fixed income, for example, can naturally create public goods when issued by governments. Public equities are well-suited to influence incremental change in large firms. Venture capital is a disruptor of business models and services. Real estate is key to the built environment. Public equities are structured to enable incremental change at the largest companies. Private equity offers opportunities to extend their typical activist positions beyond purely financial issues to those with systemic social and environmental implications, as was in the widely publicized case of Engine No. 1's engagement with ExxonMobil over its stance on climate change.

With these characteristics in mind, investors can tailor their investments to address system-level issues including income inequality. This may or may not impact the size of their specific allocation of assets to individual classes depending upon various financial considerations—and it may or may not impact their specific security selection within each asset class. But awareness of the functional capabilities built into each asset class will help them in developing an overall system-level strategy for influence. The following discussions of individual asset classes illustrates some of the ways in which investors are using these asset-class-specific design features to help increase awareness of income inequality and how society can best address its challenges.

Two broad asset classes dominate the investment landscape: equities and debt. Each offers specific avenues for influence at system levels.

Equities

Public Equities. Public equities are stocks in large firms traded on public exchanges. The market for public equities was created in part so that both large and small investors could share in these large corporations' profits while corporations could in turn raise funds from the full range of potential investors. This leads to a first benefit: companies enjoying the efficiencies of their large scale can more easily raise capital and at the same time broadly share their profits. But since the public is involved, government requires these companies to disclose their financials and business strategies. This leads to a second benefit: investors now have data on and access to companies, which can in turn be used to pressure these corporations to operate efficiently, and, in the public's long-term interests.

System-level investors use their public equity investments to set models for corporate behavior among the largest companies in the world across all industries. These behaviors are for key stakeholders and issues that, at a system level, pose risks to all or can offer such rewards.

Private equity and other private markets. Private equity consists of direct ownership by investors—individual or institutions—in for-profit enterprises. Owners, few in number, benefit from the freedom to run a firm as they choose, depending upon who has the dominant ownership and negotiated control. They are often more nimble than large public companies and can more easily effect meaningful change in company practices. They can reinvest profits in their firms or take them for themselves. They are not required to disclose their finances, business strategies, or management practices to the public.

Sustainable investors may set out to find and use private equity fund managers that incorporate social and environmental concerns at portfolio levels. By setting standards for the private equity industry as a whole, investors can raise some of the more systemic challenges that overly aggressive private-equity practices can pose, such as overburdening firms with debt, stripping out corporate assets at the expense of firms' long-term prospects for profitable operations, and charging of excessive management fees.

In addition, fund-of-funds private equity managers can, through their due diligence processes, make progress in setting social and environmental standards as well as best practices for the industry more generally. Due diligence can address aspects of measurement of positive social and environmental impacts with system-level implications for funds with holdings that address such challenges as poverty alleviation, renewable energy development, food security, and similar issues.

Fixed income and loans

Bonds, along with direct lending, form the second large class of investments. They provide enterprises and individuals with access to upfront cash that they can pay back over time. Bonds promise a regular flow of payments to their investors (the "coupon") and have evolved into a huge, diverse, and complicated asset class.

System-level investors can participate in creating and setting standards for what are essentially markets for new types of bonds. The development of the social bond market illustrates this point. Around 2013, a handful of development financial institutions began issuing what they described as "social bonds" that funded projects such as improving food security and access to education, as well as health care and financing in underserved areas. What qualified as "social," however, was not explicitly clear.[126] Rising interest led to the development of several sets of voluntary "principles" for social bonds by the financial industry, agencies, and other stakeholders. Following these principles, some trade associations now consider social bond projects to include basic infrastructure, access to essential services, affordable housing, job creation in times of crisis, food security, and socioeconomic advancement and empowerment, particularly for those living below the poverty line and the marginalized, underserved, underemployed, or otherwise vulnerable.[127]

In addition, under certain circumstances in the primary market for bonds, investors have an opportunity to advocate for the inclusion of covenants that would address systemic concerns such as income inequality or climate change, although this is far from a common practice at the current time.

A closer look: The FB Heron Foundation

The FB Heron Foundation, a private foundation that addresses various aspects of income inequality through its focus on community economic development, describes itself as operating "at the intersection of community and capital markets" and seeks to use its investments along with its grants to empower people and institutions in low-income communities.[8] In 2019, to address the disjunction between the rich agricultural corporations operating in the San Joaquin Valley of California and the poor conditions of many of their workers, it chose two fixed-income investments—loans and bonds—to support Self-Help Enterprises (SHE), a local non-profit focused on building and maintaining healthy homes and communities. Fixed income investments, especially those issued by government to support non-profits, are particularly well suited to build infrastructure and public goods that can produce positive outcomes.

Heron initially made a $1 million, 10-year below-market-rate loan (a "program-related investment") to the organization to establish a long-term base for SHE's operations. Soon after, it identified a market-rate bond issued by the California Health Facilities Financing Authority that funded two of SHE's projects, along with similar initiatives in the region. This $1 million bond became part of the Heron endowment's market-rate portfolio.

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8 For an expanded understanding of the role of grants and blended finance, see ImpactAlpha's Catalytic Capital beat. In partnership with the Catalytic Capital Consortium, the beat digs deep into the deals, people and strategies for using patient, risk-tolerant, and flexible capital.

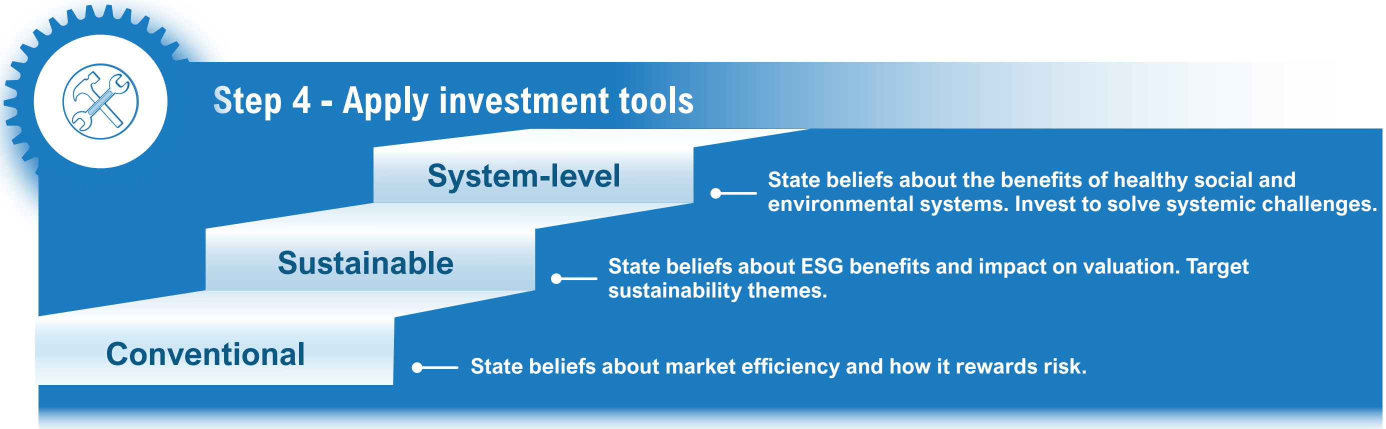
Table 3. Using asset class design for income inequality impact

	Labor and workers' rights	Executive Compensation	Taxes
Public Markets: leveraging divestment and proxy voting for shareholder influence on systemic challenges			
Public equities	The Franciscan Sisters of Allegany filed a shareholder resolution with Wendy's in support of the Coalition of Immokalee Workers' and fair labor standards for farmworkers. After initially fighting the resolution, Wendy's eventually supported it in 2021.[128]	Among the largest asset managers that voted more than 80% of the time against excessive CEO compensation packages in 2021 were: Aberdeen Standard Investments (84%), Allianz Global Investors (92%), BNP Paribas Asset Management (90%), and UBS Asset Management (89%).[129]	Norges Bank Investment Management (NBIM) divested from seven companies due to, "aggressive tax planning and cases where companies do not give information of where, and how, they pay tax."[130]
Fixed Income: using bond covenants for raising funds targeted to systemic challenges			
Agency bonds	In 2020, the European Commission began issuing social bonds under its SURE program to aid businesses and the unemployed impacted by COVID-19. The first of a projected €100 billion in these social bonds were issued to strong investor demand.[131]	At the time of writing there are few examples of fixed income investors using legal power to address these systemic social issues.	At the time of writing there are few examples of fixed income investors using legal power to address these systemic social issues.
Sovereign debt	At the time of writing there are few examples of fixed income investors using legal power to address these systemic social issues.	At the time of writing there are few examples of fixed income investors using legal power to address these systemic social issues.	At the time of writing there are few examples of fixed income investors using legal power to address these systemic social issues.
Loans	BlueHub Capital is a community development financial institution serving low-income communities and addressing income inequality as a primary goal. Its loan fund has served customers in 28 states.[132]	At the time of writing there are few examples of fixed income investors using legal power to address these systemic social issues.	At the time of writing there are few examples of fixed income investors using legal power to address these systemic social issues.
Private Markets: communicating among PE investors to set best-practice industry standards addressing systemic risks			
Private equity	The Principles for Responsible Investment (PRI) created a guide for general partners at private equity firms looking to manage sustainability issues. One of the frameworks includes the possible use of a human rights violations screen when sourcing deals.[133]	At the time of writing this report, few to no investors utilize this approach.	At the time of writing this report, few to no investors utilize this approach.
Venture capital	At the time of writing this report, few to no investors utilize this approach.	At the time of writing this report, few to no investors utilize this approach.	At the time of writing this report, few to no investors utilize this approach.

	Labor and workers' rights	Executive compensation	Taxes
	Private Markets: communicating among PE investors to set best-practice industry standards addressing systemic risks		
Real estate	GRESB maintains a Real Estate Assessment, an investor-driven global ESG benchmark and reporting framework for listed property companies, private property funds, developers, and investors who invest directly in real estate.[134]	At the time of writing this report, few to no investors utilize this approach.	At the time of writing this report, few to no investors utilize this approach.
Infrastructure	North America's Building Trades Unions (NABTU) maintains two objectives: to hold investment management firms to a high standard of business operations and to clearly indicate how such firms can improve their policies and practices in the years ahead.[135] NABTU evaluated Responsible Contractor Policies (RCP) across 10 criteria.[136]	At the time of writing this report, few to no investors utilize this approach.	At the time of writing this report, few to no investors utilize this approach.

* For the purposes of this table we've featured actions by investors in specific asset classes as they relate to the identified themes of labor and worker's rights, executive compensation, and taxes. Additional examples of investor action in specific asset classes for other social, and environmental, issues do exist. We've nonetheless limited the examples highlighted here to those that correspond to the identified issues in an effort to (a) demonstrate the need for innovation and action by the investment community, and (b) to exercise caution when drawing conclusions about the usefulness and applicability of investment structures geared towards addressing issues other than income inequality.

** One dimension not illustrated in the table is the importance of 'market influence.' While few examples exist among the three levers discussed above, market influence by investors remains a powerful tool for instituting change at a system-level for all systemic risks, including income inequality.



The challenge

A challenge for investors utilizing conventional investment tools remains the short-term perspective blinding them to the consideration of systemic, long-term challenges—challenges that exist today and will only increase in the future. Furthermore, even if an investor were to notice and wish to address these long-term issues, conventional investment tools fail to offer solutions.

Addressing income inequality, as with any system-level issue, requires long time-horizons. The good news is, many institutional investors already develop their investment strategy in the context of future liabilities (pension obligations, for example) that can range 30-50 years in the future. Similarly, individual investors often depend on their investments to support goals that will be realized far in the future. Long-term investors are likely to be sensitive to the risks of income inequality and attuned to repairing trust and relations between companies and employees or government.

In extending their horizon, however, investors will also confront a tension between investments managed to short-term and long-term objectives. Conventional investors who maximize short-term returns by investing in companies that keep their labor costs and tax payments low neglect the long-term risks of this strategy to the company and to society. At the same time, investors cannot focus solely on a firm with long-term benefits to society at the expense of returns to their funds.

While conventional investors avoid overvalued securities, sustainable investors avoid holdings or securities with weak sustainability impacts. Furthermore, they engage with their holdings to improve social and environmental performance along with financial performance.

Still, neither approach addresses the underlying flaw of systemic issues; both fall short of evaluating the effect an investment has on the larger health of social and environmental systems. Failure to do so keeps conventional and sustainable investors from applying social and environmental standards to establish system-wide norms. Instead, evaluating the effect of an investment on systemic issues requires investors to balance the short term with the long term, and the generation of private goods with that of public goods.

Opportunity for action

Many investors have already adopted “ESG Integration” as a daily practice, incorporating this approach into security valuation when they deem it material to stock price. This is a first step on the road to extending other everyday investment practices to a system level.

Four areas of daily practice lend themselves to an extension of system-level considerations (though their application will vary based on industries, companies, and asset classes):

1. Investors can be more transparent about their beliefs regarding the characteristics of financial markets to include their position on the significance, if any, of social and environmental risks to their investments across all asset classes.
2. Investors' security and portfolio risk management techniques can look beyond individual security analysis to assess social and environmental issues that have adverse or positive impacts on entire industries or on stakeholder issues that cut across all industries and portfolios.
3. Engagement with corporations can extend beyond assessing the financial implications of social and environmental challenges on the business models or stakeholder relations of individual firms to include engaging entire industries on the same topics, which influence all portfolios.
4. Finally, manager due diligence processes can evolve from assessments of managers' competencies at security- and portfolio-levels to encompass their skills at managing systemic risks.

In the context of income inequality, investors can extend their traditional investment tools from a company and portfolio focus to the broader contexts of industries and systems. To begin with, investors may already publicly state their beliefs about the efficiency of markets, or the relationship of risk and reward, or the materiality of social and environmental data. But for income inequality, investors can also specify their belief in the long-term value of the stability of the social systems upon which they depend. Such statements can help shift the fundamental mindset of the investment community. Next, they can construct portfolios that not only deemphasize companies with histories of poor labor practices and possibly engage with a few of them, but also set standards for entire industries such as footwear and apparel, agricultural products such as cocoa, bananas, and shrimp and on issues such as child and bonded labor.

A closer look: Prudential Financial

Since its founding in 1875, Prudential Financial, the global financial services giant, has called Newark its home. This has been a conscious choice by the company. Prudential is widely considered one of the anchor institutions of the city and has supported Newark's economic revitalization since the 1970s through its financial inclusion initiatives and support for underserved neighborhoods. Between 1976 and 2016, it invested $2.6 billion to impact investment projects around the world, including $1 billion to the economic revitalization of Newark through both its impact investment programs and philanthropic activities.[137]

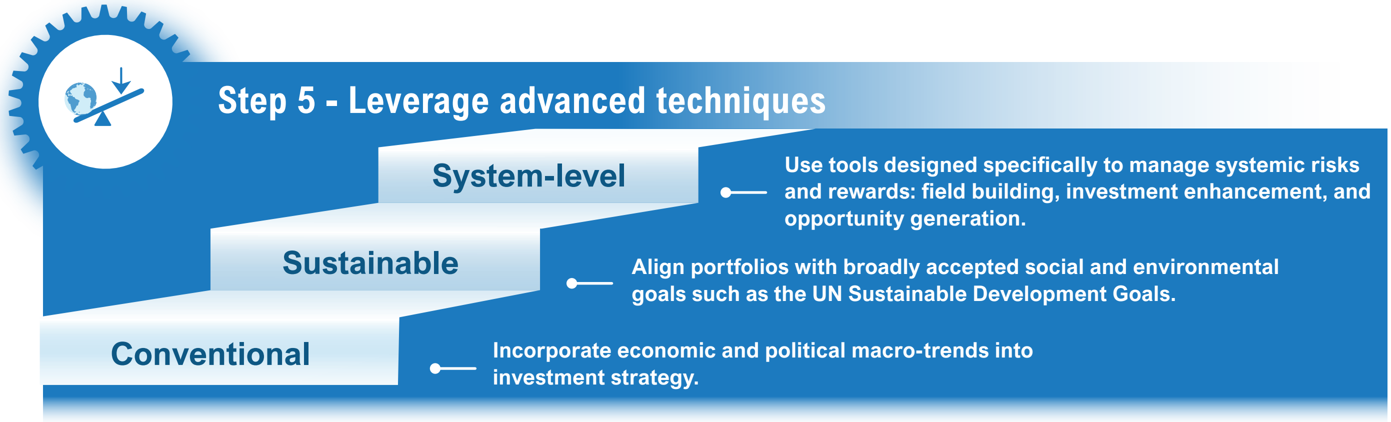
One of its subsidiaries, Prudential Global Investment Management (PGIM), operates an impact investment fund through its Prudential Impact Investing Unit (PII). This fund is an example of how an investor can extend the use of conventional investment techniques to address a systemic issue: the challenges of local poverty alleviation, affordable housing, youth training, access to capital, and income inequality.[138]

PII made $1 billion in community-focused impact investments between 2014 and 2020. PII is a solutions-oriented fund that strives to advance economic and social mobility for underserved populations. It invests in both for-profit and non-profit enterprises with a focus on promoting financial inclusion by investing in microfinance organizations, community development financial institutions in the U.S. and financial services companies in the developing world, as well as organizations promoting job training and skills development in underserved communities.[139]

Through its long-term investment in Newark, Prudential has demonstrated the power an investor has when it dedicates itself to a specific issue.

Table 4. Applying investment tools to income inequality

	Conventional techniques used at a system level	*Real-world example*
Reflecting systemic concerns in investment beliefs	Include beliefs about the potential risks and rewards of non-diversifiable income inequality risks and opportunities for rewards across asset classes.	Cbus utilizes a responsible investment policy where three of the five principles (health and safety, labor and human rights in direct operations and supply chains, and product supply chains) focus on income inequality-related issues. Specifically, Cbus believes this policy "will reduce the volatility in financial markets brought about by climate change, social and economic inequality, and unequal access to resources such as energy, water, and food."[140]
Emphasizing systemic issues in security selection and portfolio construction	Incorporate the long-term implications of income inequality, specifically labor rights, CEO compensation, and taxes, on entire industries and asset classes in security selection, portfolio construction, and asset allocation.	Aviva investors, an asset management company with $480 billion in AUM, alongside six other asset managers, refused to participate in the IPO of Deliveroo, an online food delivery company, over workers' rights issues. Aviva and the other managers refused investment due to Deliveroo classifying their riders as self-employed, meaning they would not be entitled to a minimum wage, holiday, or sick pay.[141]
Engaging with holdings about systemic issues	Extend engagement beyond company-specific engagement on income inequality, taxes, labor rights or CEO compensation concerns to entire industries to raise fundamental issues about business models and stakeholder relations.	The Committee on Workers' Capital created the Guidelines for the Evaluation of Workers' Human Rights and Labor Standards, reflecting international standards and norms (e.g., UN Guiding Principles for Business and Human Rights, OECD Guidelines for Multinational Enterprises, and ILO Fundamental Conventions). This framework recommended investors analyze companies' overall social performance against roughly 50 indicators from nine thematic areas, such as workforce composition, supply chain, pay levels, and grievance mechanics.[142]
Evaluating and selecting managers based on their consideration of systemic issues	Include in due diligence assessments of managers' thoroughness, skills, consistency in style, and performance related to income inequality risks and rewards. Extend this due diligence to financial consultants.	Following the reporting period of the Modern Slavery Act, HESTA, a $52 billion Australian superannuation fund for workers in health and community service sectors, engaged with all of its active managers on the presence of forced labor in their investment portfolios.[143]



The challenge

To exercise influence at systems levels, investors must strike a careful balance between the need for financial returns and the need to strengthen and bolster systems. Conventional investors largely focus on the financial returns of their portfolios. They translate economic and political macro-trends into their investment outlook and strategy for risk-management at this level. Their analysis does not extend to activities and techniques that can help improve underlying systems themselves. System-level investors look to the potential risks and rewards of such macro trends at both the portfolio and systems level and seek to strike a balance with their management of risks in both.

Sustainable investors can take globally established and accepted standards into account as they develop their investment strategy. However, these standards—Iris+, Value Reporting Foundation's SASB Standards, and The Global Reporting Initiative— seek to better support investors to address environmental and social factors in their portfolios, not measure the health and stability of systems.[144] While the opportunities for company-specific social, environmental, and material financial returns are quantified, without a systemic perspective, the systemic risks cannot be considered or addressed.

Balance is found in those firms that are committed to employee and labor relations, paying taxes, and appropriately compensating CEOs while still controlling costs and maintaining profitability. It is a challenging task, but investors who can strike this balance in their decision-making, and offer it as a model for others, not only create competitive investment opportunities for themselves but also a stable and sustainable financial system and society for all.

Opportunity for action

Forward-looking investors are pioneering a wide range of techniques designed to contend with 21st century system-level challenges. These techniques can be grouped according to three broad or overarching tactics—field building, investment enhancement, and opportunity generation—that illuminate the path forward for the practice of system-level investment.[145] First, investors start working more collectively (field building). Then, they change the way they make investments (investment enhancement). Finally, they create investment opportunities that will improve systems (opportunity generation).

These tactics differ from those historically used by conventional investors by stressing collaborative actions, building shared knowledge bases, and setting industry standards to create a rising tide of investment opportunities for all investors. In doing so, they focus on key leverage points that can strengthen overall systems, enhance their resilience, and ensure their long-term sustainability.[146]

Field-building techniques help investors to act collectively

No single investor can influence systems alone. Investors can use the following field-building tools to contend with social and environmental challenges, improve their communications on these issues, and help set rules of the game that facilitate their ability to protect their assets from risks and identify system-level rewards.

There are three field-building techniques: Self-organization, Interconnectedness, and Polity.

- **Self-organization:** Investors join or create collaborative organizations that can build capacity to address social and environmental systemic issues across the investment landscape.
- **Interconnectedness:** Investors increase the flow of information and communication about social, financial, and environmental systems among peers, with clients, and with the public at large to build trust and increase the alignment necessary for shared goals and collaborative action.
- **Polity:** Investors call attention to public policy debates about governmental rules and regulations that can positively or negatively impact their exposure to risks at environmental, social, and financial system levels. This aligns political activity with the system-level commitments and goals of investors.

Through these field building techniques, investors seek to collaborate, improve the quantity and effectiveness of information flows, and shape the rules of the game. In doing so, investors recognize the importance of collective action, having a shared knowledge base, and an enabling environment to manage common pooled sources of wealth creation and avoid a "tragedy of the commons."

Investment enhancement techniques influence the characteristics of a system

Once they are organized, investors can enhance the power of investment to exercise leverage within social and environmental systems.

There are three investment enhancement techniques: Standards Setting, Solutions, and Diversity of approach.

- **Standards setting:** Investors establish standards and norms that provide the basis for engagement or investment/divestment in industries as a whole or with regard to cross-cutting issues. Such techniques can change the dynamics of systems and generate positive outcomes from the outset.
- **Solutions:** Investors identify investments and promote business models that resolve pressing systemic challenges entirely, rather than profit from their continued existence.
- **Diversity of approach:** Investors use a diverse range of investment approaches simultaneously at key leverage points within a complex system to maximize their leverage in addressing systemic challenges.

Opportunity generation techniques help to strengthen systems

After investors collaboratively address the norms and dynamics of a system, they can use their investments to strengthen the social and environmental systems upon which they depend for returns.

There are four opportunity generation techniques: Additionality, Locality, Evaluations, and Utility.

- **Additionality:** Investors design and participate in the use of financial products that intentionally include addressing systemic challenges in their definition and structure.
- **Evaluations:** Investors look beyond quantifiable price and evaluate inherent worth of systemic intangibles such as natural, social, and human capital.
- **Locality:** Investors create interlocking investments in environmental and social systems within a given geographic region to strengthen resilience and value creation.
- **Utility:** Investors maximize the societal uses for which specific asset classes were explicitly created to address specific systemic challenges.

A closer look: The Council on Ethics [9]

Created in 2007 by four of the Swedish AP national pension funds to "contribute, through dialogue, to the development of sustainability work in non-Swedish listed companies," the jointly managed Council on Ethics (CoE) engages with non-Swedish companies in four major areas including human rights as related to labor and income inequality. Alongside these four areas, CoE was created to produce financial returns.[147]

The CoE has progressed from engagements aimed at improving practices at a single-company level to a system-level focus. It describes this progression as: "Our focus on engagement has over the years led us from individual companies to the entire sector and now to engaging a problem. It is a big step forward, not only for the Council on Ethics, but for the movement on responsible investments."[148]

The CoE's four primary focus areas are 1) human rights, with an emphasis on child and forced labor, health and safety and, starting in 2020, human rights issues in the tech sector; 2) climate with an emphasis on achievement of the Paris Agreement; 3) environment, with an emphasis on biodiversity; and 4) business ethics, with an emphasis on anti-corruption.[149] For each of these issues, the CoE adopts a system-level perspective and often employs several of the advanced techniques described previously.

In 2020, for example, it completed a three-year collaborative initiative with investors led by Sustainalytics focused on "systemic labor rights issues in food supply chains." In particular, it developed standards for best practices in food companies' agricultural supply chains with regards to labor rights risks, living wages, and due diligence, to measure and improve the performance of specific companies.[150]

The CoE reports that during this time it has seen countries such as the U.K., France, the Netherlands, and Australia implement legal requirements for companies to develop human rights due diligence policies, a step it applauds and an example of polity.

Starting in 2019, concern with the fatal and destructive collapses of two of Vale's mining tailing ponds led the CoE to collaborate with Church of England to form an international coalition of investors to engage not only the company but the mining industry as a whole. As a result, the industry agreed to create a publicly available, global database of major tailing ponds including details on their safety status—an example of interconnectedness.

The CoE also self-organized by collaborating with the International Council on Metals and Mining and the United Nations Environmental Program to develop a *Global Industry Standard on Tailings Management*. It plans to set up an independent institute "to oversee the implementation of the standard, but also mining dams in general."[151]

Additional examples of the advanced techniques in action follow in Table 7.

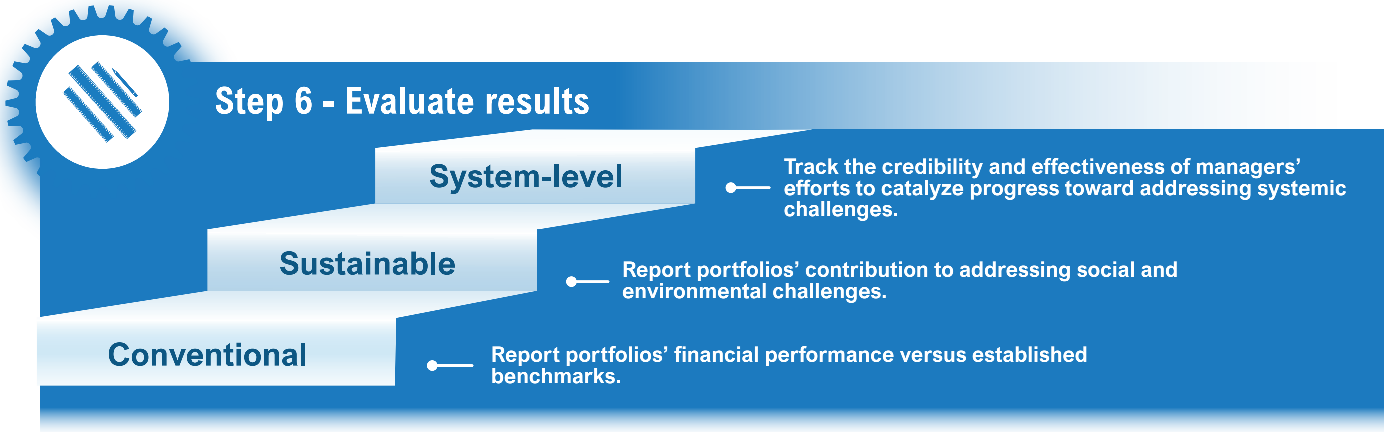
9 While The Council on Ethics is an industry leader in system-level investing, it is important to note that no single investor is using all 10 advanced techniques in their investment process.

Table 5. Leveraging advanced techniques to address income inequality

		Income inequality
Field Building	*Self-organization*	Investors are increasingly joining coalitions to augment their influence on corporate levels, particularly around income inequality. For example, on taxes, 11 major investors, including Bâtirente, MFS Investment Management, NEI Investments, RobecoSAM, and Triodos Investment Management, joined the Principles for Responsible Investors' taskforce on taxes, which issued a guide on the why and how of engaging with corporations on this issue.[152]
Field Building	*Interconnectedness*	Investors are increasing the flow of information and communication about income inequality with peers, initiatives, and the general public. ShareActions's Workforce Disclosure Initiative (WDI) focuses on improving accountability and corporate transparency on workforce issues. WDI provides its 49 members (companies and investors) with comprehensive and comparable social risk data; in 2019, WDI collected data from 118 companies in 11 industry sectors across 17 countries. This data covered companies' direct operations and their supply chains via a 180-question survey covering 10 thematic areas such as occupational health and safety, workers' rights and composition, and compensation.[153]
Field Building	*Polity*	Investors continue to set more comprehensive standards around income inequality to promote more thorough data disclosure while simultaneously pushing for disclosure to be mandatory and standardized. For instance, the UAW Retiree Medical Benefits Trust helped organize, and still houses, the Human Capital Management Coalition (HCMC). Supported by 32 institutional investors with $6 trillion in AUM, HCMC petitioned the Securities and Exchange Commission in 2017 to require company disclosure of human capital management policies and practices. HCMC asserted such disclosures were "fundamental to human capital analysis," and included workforce culture and empowerment, workforce health and safety, human rights, and workforce compensation and incentives in their disclosure requirements.[154]
Investment Enhancement	*Standard setting*	Investors have established standards that discourage investments in industries and countries with practices that violate broadly accepted standards or norms around income inequality, or contribute to the development of such standards. For instance, the Cleaning Accountability Framework (CAF), a multi-stakeholder coalition of investors (including Australian Super and AMP Capital), unions, real estate developers, facility managers, academic institutions, and the Australian government's Fair Work Ombudsman department. CAF promotes RCPs to protect the rights of workers who are providing cleaning services to properties owned by institutional investors. Among its activities, CAF provides its members, including investors, with a Code of Conduct and a procurement toolkit with industry- and market-specific pricing and quality-of-service benchmarks. To encourage the adoption of the standards, CAF has a certification and rating program for contractors.[155]
Investment Enhancement	*Solutions*	Investors continue to invest in enterprises to solve the challenges of income inequality. These investors can address workers' rights and financial and political equity both individually and in partnership with peers. For example, the Isibaya Fund is a division of the Public Investment Corporations, the largest investment manager on the African Continent. The Isibaya Fund invests in high impact areas for socioeconomic development that bring financial returns and social dividends to the country. The Fund's areas of focus include Black economic empowerment, renewable energy, healthcare, education, and other infrastructure development projects that help to create jobs, relieve poverty, and transform the economy.[156]
Investment Enhancement	*Diversity of approaches*	Investors are using a diverse range of investment tools to address the complex challenges of income inequality. CCLA Investment Management, a manager for charities, religious organizations, and the public sector, has convened Find it, Fix it, Prevent it, an investor initiative with nearly $10 trillion in AUM to mobilize the U.K. investment community to work against modern slavery. This initiative aims to promote public policy, increase corporate engagement, improve data disclosure, and commission a new rating tool – all through a coalition of 56 supporters, such as Australian Super, Fidelity International, and Schroders. Further, this initiative coordinates between investors, NGOs, and academics to develop data points around modern slavery, then lobbies ESG data houses to include them in standard rating products and work with governments.[157]

Table 5. Leveraging advanced techniques to address income inequality

Opportunity Generation		Income Inequality
	Additionality	Investors create financial products that intentionally address social inequalities and social and environmental market failures that ultimately decrease the resilience and stability of social, financial, and environmental systems. For instance, Bridges Fund Management targets opportunities that create jobs and improve the skills of workers, such as vulnerable young people and aging populations. Bridges also promotes healthcare in historically underserved communities while emphasizing sustainable living.[158]
	Evaluations	CalPERS is the pension fund for the civil service employees of the State of California. It believes that "Long-term value creation requires effective management of three forms of capital: financial, physical, and human." Among the essential aspects of human capital management in long-term value creation, it includes "fair labor practices, health and safety, responsible contracting, and diversity"—all considerations that factor directly into stock price valuation but nevertheless have intrinsic value that is difficult to quantify.[159]
	Locality	To strengthen the health of social systems, investors can invest to decrease the level of income inequality in a given city, state, region or country. For instance, Prudential Impact Investing Unit (PII), an impact fund operated by Prudential Investment Management (PGIM), has made over $1B in community-focused impact investments between 2014 and 2020 in Newark, New Jersey. These investments were made to bolster underserved populations in Newark, promoting economic advancement and social mobility.[160]
	Utility	Investors can reduce levels of income inequality by maximizing the alignment of specific investments within a portfolio's asset classes with the social functions that these assets classes were designed to serve. For example, the Heron Foundation, a private foundation focused on community economic development, utilized two fixed-income investments, loans and bonds, to build affordable housing in communities in the San Joaquin Valley of California. These two investments, especially when issued by governments to support non-profits, significantly promote the building of infrastructure and public goods. These investments later resulted in a more stable community, further loans from other entities, and the stabilization of Self-Help Enterprises, a local non-profit focused on building and maintaining homes.



The challenge

All investors with system-level aspirations face a number of sticky questions: *How can we know which financial products and services and which asset managers are truly addressing the major systemic challenges of our times? Who is simply insulating their portfolios from the adverse impacts of ever-increasing harm to our environment and society? Who is serious about fighting income inequality or climate change vs. engaging in "greenwashing" with misleading claims and empty gestures?*[161]

Conventional investors evaluate performance against certain established benchmarks and assess a manager's contribution through a portfolio's overall performance. Sustainable investors go deeper to assess the '5 dimensions of impact' (the what, who, how much, contribution, and risk) when addressing social and environmental challenges.

Recent developments, including adoption by investors of the UN SDGs, are forcing the question of what it means to realize progress towards systemic goals—and that requires a systemic evaluation approach. The SDGs are clearly ambitious and address challenges at the system level.[162] As more and more managers align themselves with them, investors want to distinguish who is best at doing so. To make such assessments, they need a practical and comprehensive impact measurement framework—one that can separate those genuinely and effectively committed to solutions and influence at system levels from those simply protecting their portfolios against specific risks, or worse yet, from the cynical "greenwashers" of this world.

Opportunity for action

Today's conventional investors have a well-established discipline for comparing the performance of one manager with another. This familiar, five-part framework assesses managers' investment philosophy and their process, the financial expertise of their staff, their discipline in portfolio creation, and the financial performance of their portfolios relative to that of their peers and established benchmarks.

Because this conventional due diligence approach does not assess the social and environmental impacts of their holdings and portfolios, sustainable investors have had to confront the difficult question of how to measure that impact. Over the years, great progress has been made in addressing this challenge. Still, incorporating due diligence on managers' skills and accomplishments managing systemic risks and rewards remains an unanswered challenge.[163]

We propose four basic principles that investors will want to consider when designing their evaluations of investments for social and environmental returns. Specifically:

- **Consistency is essential.** All three links in the investment chain (managers, their actions, and their outcomes) must be evaluated. Without consistent commitments to sustainability at all levels, greenwashing, or its appearance, is likely.
- **Judgment is valid.** The ability to measure progress toward sustainability goals requires qualitative judgment as well as quantitative metrics.
- **Inherent worth has value.** Effective evaluations integrate the inherent worth (i.e., the long-term, intangible value) of social and environmental systems along with their price-based attributes. Reliance on price only as a measure of value is inevitably short term. Incorporation of the difficult-to-measure inherent worth of these systems helps investors maintain long time-horizons.
- **Balance is crucial.** Investors must balance the long term with the short term and the creation of public goods with private benefit. They live in a world of markets driven by short-term valuations and are simultaneously sustained by foundational social and environmental systems. The skillful management of the competing demands of these two factors is the essential challenge of evaluating sustainable and system-level investments.

A proposed six-part framework for evaluating system-level progress on income inequality follows in Table 8.

A closer look: The Jessie Smith Noyes Foundation

The Jessie Smith Noyes Foundation is a family foundation with a mission of promoting social justice. As far back as the 1990s, Noyes had adopted a comprehensive program of impact investment initiatives. These went beyond simply screening out bad actors in public equity portfolios to include program related investments and social venture capital, with an emphasis on regenerative agriculture and community economic development.[164]

In 2016, when Noyes began a search for external managers, it faced a new challenge, one that was emerging for investors concerned with sustainability: who among the growing number of asset managers purporting to offer sustainability products had a true commitment and deep expertise?

In issuing the Request for Proposals (RFP), the foundation asked typical due diligence questions around managers' experience, investment processes, and expertise, as well as their knowledge of and fluency in sustainable investing. The foundation also wanted to understand the ability of the manager to help facilitate the full activation of Noyes' assets "to create long-term, systemic change."[165] To this end, Noyes included the following questions:

> *How can our mission-aligned investment portfolio drive the creation of systemic impact in the areas of social justice, equality, human rights, health, and diversity? Are there external initiatives or targets—such as the United Nations Sustainable Development Goals (SDGs)—that might influence our portfolio?*[166]

Table 6. Framework for evaluating system-level progress on income inequality

	System-level best practice
Do the investors have formal beliefs or principles that are sufficiently clear, actionable, inspirational, and adaptable to be effective?	Managers should clearly state their beliefs and principles with regard to system-related social or environmental challenges. They might, for example, develop an Investment Beliefs Statement (IBS) or principles regarding the materiality of the systemic risks posed by climate change across asset classes. They might also confirm their belief in the inevitable impact, positive or negative, of their investment decision-making on climate change, their ability to manage that impact, and their responsibility to do so. Managers can state these in an IBS, Investment Policy Statement, stand-alone sustainability report, or other forms of public reporting.[167] These beliefs and principles can then provide the overall guidance for evaluating managers' actions and outcomes. They can help answer the question: Have managers acted consistently with their stated beliefs, and are they likely to do so in the future? These beliefs and principles should serve as guidelines for future decision-making under varying circumstances and market conditions and help ensure consistency going forward.[168]
Can investors justify their selection of the systemic challenges they have chosen to focus on?	Evaluating the adequacy of a manager's rationale for focusing on a particular system-related social or environmental challenge can assure the investor that conflicts of interest, frivolous endeavors, or otherwise idiosyncratic, personal, or political agendas are not involved. Managers should only undertake a system-related approach in cases of broad, universally recognized systemic risks or rewards.[169] Without justifications, investors cannot make judgments about the appropriateness of managers' decision to focus on a particular issue.[170]
Have the investors chosen and skillfully used techniques designed to create impact at the system level?	Evaluating managers' choice of techniques can help investors understand whether they have sufficient knowledge to exercise influence within complex systems. If managers do not choose well or skillfully, they have little prospect for achieving impact.[171] Properly selected and applied, these techniques (referenced in this guide) can act at leverage points within a system to create impact, especially when the interests of stakeholders align with the goals of the system itself.[172]
Have the investors applied those techniques at key leverage points within the system in ways that exercise positive influence?	Evaluating managers' choices of key leverage points helps investors understand whether their actions are likely to exercise influence effectively and efficiently. Investors can evaluate the appropriateness of their managers' choice of leverage points at which to intervene, as well as the ambition and intensity of that intervention.[173] Managers who understand leverage points can see where they have the most impact and then can focus on that point. For income inequality, they may engage in collaborative action with other investors, take up public advocacy, embrace communication of relevant data, or reconceive market mechanisms—because each of these may be effective leverage points for shifting current paradigms of workers' rights, CEO compensation, and taxes.
Have the investors' actions generated desirable outcomes?	Evaluating progress toward systemic goals helps investors judge the effectiveness of managers' contributions. Investors that measure managers' impact with respect to system-level change can focus on two areas. First, their managers' contributions to commitments by their peers in the investment community, along with corporations and even governments, to a common goal for system-related change; for income inequality, for example, commitment to policies consistent with a living wage.[174] Second, investors can look at whether managers have contributed through their investments and leadership to catalyzing collaborative actions to building the infrastructure needed to promote system-related change.[175] Again, for income inequality risks, owners could evaluate managers' investments and other initiatives that support jobs honoring workers' rights and protections and, in an organizational context, the creation of collaborative initiatives to promote fair labor standards.
How have the investors contributed to positive, paradigmatic shifts within the system itself?	Managers cannot exercise effective influence if the interests of the key stakeholders in the system in question are not aligned. However, managers can improve alignment on two levels: the interests of managers and the interests of key stakeholders within the overall system. Both can be difficult to achieve. Communications and trust are key prerequisites to encouraging such alignment.[176] Investors may, therefore, wish to assess how and to what degree managers' actions have contributed to alignment of interests. Regulatory action is the quickest and most certain way of achieving such alignment but a careful balance of regulatory action and voluntary initiatives is needed to ultimately ensure an alignment of interests throughout a complex system.[177]

Conclusion

Income inequality is a defining issue of our time. It is a system-level problem, fundamentally affecting markets, societies, politics, and people. While unfettered markets did not create income inequality, they have driven naturally occurring differences in income to unprecedented and unsustainable levels.

The level of inequality seen today has the potential to destabilize entire systems, wreaking havoc on financial systems and market stability. At the same time, income inequality introduces social instability, deepening inequities already experienced by women and racial and ethnic minorities. In a global society where the top 1% has more than the bottom 90% combined, economic growth will slow, mobility will decline, and social cohesion will deteriorate. Weakened governments will struggle to meet increasing demands for social services while contending with fewer resources.

Still, there is hopeful news. Investors are making a difference in seemingly entrenched systemic issues like income inequality through system-level stewardship. Building on the practices of conventional and sustainable investors, system-level investors are taking bold action, together, to reshape social and environmental systems to benefit society and strengthen returns. While governments play a critical role in this process, investors are essential; they can use the leverage of their capital to accelerate far-reaching changes in corporate behavior and incentives.

Investors using the step-by-step process for system-level stewardship laid out in this guide can proceed with confidence in their actions. While this guide is focused on income inequality, the stewardship process herein gives investors the tools necessary to engage with other system-level challenges such as climate change or a public health crisis. This work is challenging and evolving, but vanguard system-level investors have provided a roadmap for others to follow.

Although taking a long-term, holistic approach to investment may feel counterintuitive to some stakeholders, fortified financial and social systems lead to healthier societies and stronger long-term returns across all asset classes and investments. By focusing on system-level stewardship, investors create a rising tide that benefits all people.

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About TIIP

The Investment Integration Project's (TIIP) mission is to help investors understand how healthy environmental, social, and financial systems can benefit their portfolios. TIIP provides consulting services, applied research, and a turnkey solution that support investors' pursuit of system- level investing, an advanced sustainable investing approach that focuses on managing systemic risks and investing in solutions to systemic problems. For more information, visit https://www.tiiproject.com.

About Generation Foundation

The Generation Foundation is a UK registered charity and was established alongside Generation Investment Management LLP, the sustainable investment firm founded in 2004. Our mission is to drive the urgent transition to an equitable society in which global temperatures do not exceed 1.50C. We operate a proactive grant-making and research programme that focuses on four priority areas: investor climate action; carbon pricing; gender inclusion and empowerment; and action on economic inequality. For further information, please visit www.genfound.org.

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