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### **E#3: EQUALITY AND INCLUSIVE GROWTH**

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*“Inclusive growth is economic growth that is distributed fairly across society and creates opportunities for all.”<sup>38</sup>*

The world has made significant progress in reducing extreme poverty. There are 1.1 billion fewer people living on less than USD 1.90 a day today than in 1990.<sup>39</sup> Nevertheless, poverty rates have declined unevenly, with more than half of the world’s poor living in sub-Saharan Africa.<sup>40</sup>

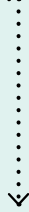
Inequality in the world has also declined consistently since 1990, but only when looking at global inequality of incomes. Inequality within many countries is increasing, especially in developed ones. More disturbingly, poverty increased significantly in Europe and the United States because of the social effects of the economic crisis until 2012, when poverty levels started to fall. However, the number of citizens living in poverty is still higher, although only slightly so in the case of Americans, than before the financial crisis struck.<sup>41</sup> In 2016, 40.6 million Americans were living in poverty<sup>42</sup>, while 23.5% of the EU population were at risk of poverty or social exclusion.<sup>43</sup> Those Europeans in the lowest income decile have lost some share of total disposable income since then.<sup>44</sup>

While intrinsically related, inequality of opportunity is perhaps more insidious, and more entrenched. It occurs when people’s place of birth, gender, ethnicity or parental background determine to a significant degree their access to education and the qualifications they obtain, their access to work and the type of job they get; and, ultimately, their level of income.<sup>45</sup> There is significant inequality of opportunity across world populations, but also in Europe and within European countries. When we look at health and education, we see large differentials in the ability of people to access basic services. Rising income and opportunities for the lower and lower-middle income households has become a serious challenge over the past decade. This has fuelled discontentment, accentuated in

times of stress for welfare services, given ageing populations, migration and the fiscal consequences of the financial crisis. In addition to being ethically unjust, inequalities of opportunity based on discrimination are a form of market failure, leading to a systemic misallocation of resources. The IMF has warned about how damaging rising income inequality can be for economic growth.<sup>46</sup> Over the past 30 years the higher inequality levels experienced in OECD countries has damaged growth rates, limiting opportunities for the poor to invest in their education.<sup>47</sup>

Climate change is also a significant driver of inequality, hitting vulnerable populations the most and reversing hard-won development gains<sup>48</sup>. It is critical to scale-up investing in adaptation, resilience and ensuring that the shocks of climate change do not disproportionately affect particular segments of society. This entails a stronger focus on the needs of the populations most affected by climate change, granting them access to the tools they need to adapt and cope with climate-related disasters. Disaggregated data on the anticipated local impacts of climate change and on the potential socio-ecological effects of responses to climate change (e.g. maladaptation risk) is a prerequisite for effective and just climate action.

The political consequences of rising inequality and social exclusion are beginning to be felt. The failure to equitably distribute the gains from globalisation and capitalism is perceived by many economists as a root cause of the so-called “populist” backlash we are seeing around the world. The changing political landscape – and the policies that could emerge alongside – could also negatively impact the foundations of democracy. As a consequence, inequality has risen to the top of the policy agenda.



## JUST TRANSITION

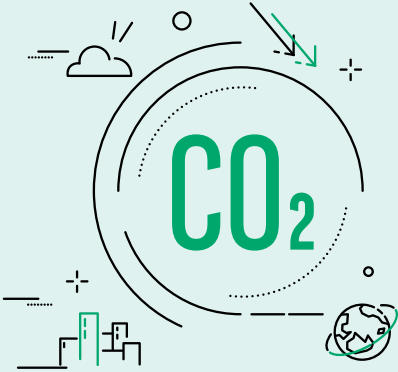
Sustainability and inclusivity go hand in hand. Limiting temperature rises to well below 2°C is a human imperative, and the best preventive measure to seriously address social challenges, not least to reducing poverty, conflict and migration and to preserving the livelihoods of hundreds of millions of people. The loss of biodiversity will also affect people living in poverty more because they depend more directly on natural capital given their limited ability to purchase (e.g. food, medicines, insurance).<sup>49</sup>

The shift to a zero-carbon and environmentally sustainable economic model is necessary, considering what is at stake. There is little doubt about the important economic and social benefits that the transition can deliver. The latest report of the New Climate Economy, for example, concludes that low-carbon growth could deliver economic benefits of USD 26 trillion by 2030 and generate over 65 million new low-carbon jobs.<sup>50</sup> Investors will have a key role to play in enabling a just transition to low-emission, climate-resilient economies. Options for investor action include,

*inter alia*, incorporating “just transition” principles in their investment beliefs, climate action plans, investment research and strategies. Of equal importance is the need for investors to work with policymakers and governments to ensure inclusion of just transition principles in national plans and long-term climate strategies.

However, and given the urgency to act, it will not come without a cost. There will be companies and sectors that will experience significant disruption. If not well managed, it could bring unemployment and economic depression to some regions.

We investors can play a critical role by ensuring that the social dimension is well-integrated in our investment analysis and decision-making, and in our engagements with companies and policymakers. We are committed to bringing the E and the S dimensions together, and to taking action to support the Just Transition by integrating workforce and social dimensions into our climate practices.<sup>51</sup>



## EQUALITY AND INCLUSIVE GROWTH: OBJECTIVES AND TARGETS

**Our objective is to promote a more equitable and sustainable distribution of value to ensure the long-term stability and resilience of societies and ecosystems. We have set three targets to advance this overall objective:**

**-1-**

To ensure that senior corporate management teams are appropriately incentivised to prioritise the success and long-term sustainability of their businesses through reform of executive compensation and the mitigation of excessive CEO-to-median employee pay ratios.

**-2-**

To encourage companies to promote all forms of diversity, and provide greater opportunities for women, and minorities, at all levels of the organisation.

**-3-**

To encourage companies to adopt more transparent tax strategies.

Investors can play an important positive role by incorporating a 'social equity' bottom line into their investment analysis and practices, and by encouraging companies to take account of and manage their labour and employment practices and impacts well.<sup>52</sup>

Companies can create opportunities for more inclusive and sustainable societies in many ways. One such way that companies can support economic development is through the payment of fair and equitable taxes – particularly when taxes are paid where value is created. These payments enable government spending on social welfare, health, education, infrastructure and R&D, all of which underpin future corporate profit growth and technological innovation. Short term strategies

based on aggressive tax minimisation can lead to capital misallocation, leave company corporate profitability and cash flows vulnerable to tax and regulatory regime changes, and may undermine long term investment returns.<sup>53</sup>

Companies can also strive to source locally; to create positive spill-overs such as through technology transfer; and to invest in the communities in which they operate. They can contribute to inclusive labour markets by investing in human capital, providing equal opportunities to women and minorities; and ensuring they uphold their obligations to respect human rights and contribute to remediating human-rights abuses to which they might have contributed.

Finally, companies can make a difference by ensuring they remunerate their employees in a fair and transparent way and equally for the same job. They can help minimise the widening gap in compensation between the C-suite executives and workers, in particular in large public companies<sup>54</sup>. Companies that share sensibly the creation of value across their organisations exhibit higher levels of retention and attracting talent.<sup>55</sup>

Today, in the midst of growing wealth and income inequalities, key questions are being asked about how capital is distributed within and across the corporate enterprise and society, from the CEO to the average employee, consumer, government and shareholder. There is also a growing focus on the role companies play in seeking to influence the 'rules of the game' through lobbying or other political activities.

We believe that the answers to these questions will help to provide an outline of the sustainable company of the future, and will help to re-balance the inequalities of wealth, income and opportunity that currently threaten the long-term stability of our economies. We will work to answer these questions and to act upon these answers, through proxy voting and direct engagement with companies, as well as research and public advocacy. In particular, we will engage with policymakers and regulators to better align financial regulations and other policies with the goals of an inclusive society. Investors have been a key beneficiary of corporate largesse. It is incumbent upon us to re-tilt the playing field in favour of a more equitable and sustainable economy.



BNP Paribas Asset Management is the source for all data in this document as of March 2019, unless otherwise specified.

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