

Future of the Corporation |

Changing Climate for Business

Output of a Business Breakfast held on 13th July 2017

BY LORD STERN

INTRODUCTION FROM COLIN MAYER

This business breakfast was the seventh of a series held as part of the British Academy's programme on The Future of the Corporation, a major research and engagement programme designed to inform the development of a new model for purposeful companies in the 21st Century. Business is a major contributory factor to climate change – but can it also offer a solution? Lord Nicholas Stern, former President of the British Academy, explores the reasons for hope and pessimism for corporations in the era of climate change, before leading the audience in discussion.

LORD NICHOLAS STERN

I will try to offer a mixture of hope and worry because they are both there in big measure. There are many good things happening, and many to worry about. I will try to blend those in a reasonable way. As I step down as PBA next week, it is particularly appropriate to link to the role of public discussion, research, scholarship, and intellectual seriousness in public life. Before we dive down into climate change, bear in mind these two things: How do we bring ideas, scholarship, and research to public life in a constructive and helpful way? What does all this mean for the role and function of corporations, and how ought corporations respond to climate change?

THE ROLE OF THE FIRM

Helping to shape public policy.

Climate change, as we argued in the Stern Review, is the biggest market failure the world has ever seen.

A market failure of this size has so many consequences that we have to fix it. That is the pro-market way of looking at it.

You cannot do all of this, or anywhere near it, through central planning and direction. Because this is so pervasive and big, and because we live in a world run in large measure through the private sector, the first thing to recognise is that public policy has to come from collaboration between private and public sectors. Professors of economics can go and try to persuade finance ministers and sometimes we do okay. But it is nothing like firms coming together and telling finance ministers, 'if you want the world economy to strengthen and move in a positive direction, this is what you have to do'. Taking the massive economic opportunity that sustainable business presents is what I would describe as the growth story of the 21st century.

Leading by example.

Corporations can also lead powerfully by example. As a corporation, you should not confine yourself to walking into the minister's office and saying, 'Put the policy in place, and then I will respond.' Much better if you show what you are already doing. Firms are already doing a great deal, all the way from cleaning up their supply chains like Unilever and Walmart, through to internal prices for carbon. Professor Joseph Stiglitz and I published a report at the end of May for the Carbon Pricing Leadership Coalition, arguing that to deliver on the Paris Agreement, together with other policies, you need to price carbon at \$40 to \$80 a tonne by 2020, and \$50 to \$100 a tonne by 2030. To drive policy forward and to achieve the goals, we need to see many more of those strong examples.

Public policy must include research and development with a leading role from the private sector. There is a good, stable rule, one that the British Academy, the Royal Society, and others have put to government, which says that \$1 for public R&D usually multiplies to about \$2 for private R&D. Country to country, this is quite a stable multiplier. We pushed a promise to make use of that multiplier into the Tory manifesto, whatever that is worth now. We worked very hard to get a promise to increase R&D in the economy as a whole (public plus private) to 3% over the medium term. It might well stick.

Again, *corporations* can be effective in pushing for R&D investment. They can work to make the multiplier as big as possible. As Feike Sijbesma, chair of the CPLC and Dutch business leader, put it: 'I am future-proofing my firm. Whether I am altruistic or not, this movement is coming. My firm had better be ready for it'.

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– Feike Sijbesma, Chair of the Carbon Pricing Leadership Coalition and CEO of DSM

The dangers of being unready as a firm constituted the motivation of Mark Carney and Michael Bloomberg in their financial disclosure recommendations, which came out at the end of last year. They said that financial institutions should look at what they hold, and report on the carbon risk and climate risk therein. Part of this could be in their buildings around the world likely to be overcome by floods or hurricanes. And they should particularly report on their robustness relative to policy moving in a sensible direction, changing the market value of firms in a potentially strong way.

Sijbesma talks of futureproofing his firm. Bloomberg and Carney say that we need that financial risk reporting because, as investors and people concerned with the stability of the financial system (and Chair of the Financial Stabilities Board in Mark Carney's case), we must ask whether firms' strategies and plans can withstand the policy changes that we need.

Lastly, if firms want high-quality students leaving universities and coming to work for them, they will have to show that they are serious about their social responsibility. This generation is deeply worried about the social responsibility of the places where they work, and rightly so. Shareholders worry about that. Investors worry about

that. That is another way in which firms can explain why they are doing what they are doing. Social responsibility is not just an ethical demand; it is an imperative for any corporation which wants to foster sound investment and quality recruitment.

THE POSITIVE SIGNS: THE FUTURE OF CORPORATION AND CLIMATE

1. **The Paris Agreement** – 2015 was quite remarkable, with the adoption of the Sustainable Development Goals in September in New York at the United Nations' General Assembly. In December, we then had the Paris Agreement. For the first time for 70 years since the end of the Second World War, we have a global agenda, agreed by everybody – 193 countries for the SDGs and 195 countries for Paris COP21 – and applying to everybody. The United States has not yet withdrawn, but the President has announced his intention. I will come back to that.
2. **A Truly Global Agenda.** This means a powerful, forward-looking agenda. After the Second World War, we developed the United Nations, the Universal Declaration of Human Rights, the Bretton Woods institutions. We had a very specific and important goal of reconstruction and development. Now, more than 190 countries are looking forward together, creating new agendas – this is much deeper and more subtle than reconstruction. How are international institutions and governance performing in relation to this global agenda we have established as a world, carefully and after a lot of thought, in 2015?
3. **Through to 2016.** The Paris Agreement came into force, ratified by 153 countries. That took 11 months – Kyoto took about eight years. You will recall that, also in 2016, the United States elected President Trump. Yet nineteen of the G20 said, in May this year, that Paris was irreversible, and irreversible is a very strong word. I was in Marrakesh for COP 22 last November, days after Trump was elected. Country after country stood up and said, 'We carry on'. So too many states, cities and firms in the USA. One of the foundations of Paris and the commitments we have seen is the understanding of the attractiveness of the transition to the low-carbon economy. It offers:

cities where you can move and breathe and be productive, and ecosystems which have some chance of survival, sound like a good idea even if you have never heard of climate change.

This is the growth story. In the short to medium term, sustainable infrastructure boosts demand and improves supply. We are already seeing the beginnings of, in the medium term, a quite extraordinary Schumpeterian period of discovery, innovation, investment, and growth.

4. **Into the long run.** On current trends or best guesses, we are headed for three degrees increase and more. You are not going to have a thriving world economy at three or four degrees centigrade. Given this, given the catastrophic effect of a three

or four degree increase on nearly every industry, sustainable business is the only long-run growth story on offer. It is a most attractive way of going forward. We passed the Trump test – states, mayors, firms, who have said, ‘We carry on’. For them and for us, to carry on is not only the responsible thing to do. It is the attractive thing to do.

5. **Changes across the world.** China may well have peaked its energy consumption. President Emmanuel Macron is pushing for no internal combustion engines on the road after 2040. Volvo are not making any solely internal combustion engine cars after 2019. India does not need to complete the coal-fired power stations already under construction. The change in India and China has been quite remarkable. Of course, pollution has been a big part of that story, but it is deeper. It is about the kind of cities that you want and how wasteful you are planning to be.

What we have seen since the election of Trump is not simply a political reaction to his stance on climate change, but the culmination of strong climate action and a deepening understanding over a few years.

That is the end of the optimistic part of what I wanted to say.

WORRYING SIGNS: THE FUTURE OF CORPORATION AND CLIMATE

The scale of what we have to do now is quite daunting. We will double the world economy, and much more than double world infrastructure, in the next two decades. The world will go from roughly 50% urbanised to roughly 70% urbanised by mid-century – from just above 3.5 billion in towns and cities, to around 6.5 billion or more in towns and cities in 35 years from now. This is a once-in-human-history urbanisation.

If a new world economy, and the new lot of infrastructure, looks anything like what we have now, we will be in deep trouble. The next 20 years is the period when we need to cut emissions absolutely by 20% if we are to have much of a chance of well below two degrees. That is the worry: the pace of change. That is why leadership is so important now.

Investment over the next 20 years will shape our future. The decisions and policies which shape investment over the next 20 years are right now.

There is an enormous sense of urgency here. That is why I worry. I am deeply optimistic about what we can do. We can do it. The key, then, is will we do it? That is about political decision making.

CONCLUSIONS

If any of this is to work, firms must broaden their horizons, and ask what the firm is for. It is not just to make profits. The deeper questions are: who are its stakeholders and what are their desires, interests and responsibilities? And stakeholders are much more than the shareholders. Why is it there? As John Kay put it – the purpose of human beings is not to breathe. They breathe in order to do the other things they do. The purpose of corporations is not necessarily only to make short or medium run profits. This is not simply about the survival of firms in a changing environment, but about what they *should do*. That is the story of the corporation under climate change.

That is the story of the future of the corporation.

DISCUSSION POINTS

The audience discussed a range of points, including:

- How firms might take a **longer-term view** in a world structured around short-term targets, from government intervention to restructuring the role of company boards.
- The difficulty of **poverty eradication** while remaining climate-conscious.
- The role of the **smaller company** in corporate approaches to climate change.
- The possibilities for **capital investment** in research and development.

NEXT STEPS

The *Future of the Corporation* initiative was launched on the 28th of September. Through to early 2020, a £1.6m research and engagement programme will aim to provide an evidence-base and recommendations to help equip business with the tools it requires to become one of the most powerful forces for creating prosperity for everyone within a sustainable world. By convening a range of business stakeholders, the Academy intends to be a positive and proactive partner in this movement to help redefine the corporation for the 21st century.

SPEAKER PROFILES

Colin Mayer is a Fellow of the British Academy, the Lead Academic on the British Academy's Future of the Corporation programme and a Professor of Management at the Saïd Business School. Colin was chairman of Oxera Ltd. between 1986 and 2010 and was instrumental in building the company into what is now one of the largest independent economics consultancies in Europe. He was appointed CBE in the 2017 New Year Honours for services to business education and the administration of justice in the economic sphere.

Nicholas Stern is leading British economist and academic. Since 2007 he has been the IG Patel Professor of Economics and Government, and Chair of the Grantham Research Institute on Climate Change and the Environment at the London School of Economics and Political Science. As head of the Government Economic Service, he led the ground-breaking Stern Review on the economics of climate change. He was President of the British Academy until July 2017.

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We are an **independent Fellowship** of the best UK and international scholars, elected for their depth of knowledge and outstanding research.

We are a **voice** for our disciplines, exchanging knowledge and ideas through a range of public events and publications; and helping to influence and shape public policy.

And we are a **funding body**, supporting research in fields from archaeology to economics and from psychology to history – producing insights and ideas that contribute to social and economic wellbeing and the cultural fabric of society.

The humanities and social sciences are integral parts of the UK's world-leading science and research base. The British Academy promotes their role in expanding human knowledge and understanding and helping address the great challenges of our time, from climate change to terrorism, and from the ethics of new technologies to the education of the next generation.

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