

# THE SRI CHRONICLES

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## News | p.3 THE ENVIRONMENTAL AND SOCIAL COSTS

OF AI STIR DEBATE

From an academic point of view | p.4 et 5 FAMILY FIRMS AND CARBON EMISSIONS

#### EDITORIAL



JEAN-PHILIPPE DESMARTIN Head of the Responsible Investment Team



# FIELD INITIATIVES ARE GAINING MOMENTUM... LEAVING REGULATORS BEHIND

This autumn is proving very busy on the sustainability news front. Climate change, biodiversity, inequalities, artificial intelligence... On the ground, initiatives and actions are flourishing, led by citizens, NGOs, and companies as well as by investors.

In these chronicles, we shall address topics that are currently stirring debate: how will artificial intelligence impact sustainable finance players? What is the new Nature 100+ initiative that we have joined as a founding member? How are family-owned companies responding to the challenges of climate change? And are we heading towards a world without work?

Meanwhile, regulators are fumbling along, both in Europe and in other regions. The European Commission recently announced it intended to conduct a drastic review of the SFDR - which could have major implications for the entire sustainable finance framework (Taxonomy, PAI etc.). On the other side of the Atlantic, the SEC (Securities and Exchange Commission), the Federal body responsible for regulating and controlling financial markets, is caught in the middle of the political and ideological battle opposing Republicans and Democrats over ESG.

Ultimately, the road to pragmatism and success could come from countries like the United Kingdom and Switzerland, which are forging ahead, trying to leverage what works best on both sides of the Atlantic, and globally (ISSB).

Highlights this autumn include the next COP summit at the end of November in the United Arab Emirates. On this subject, let me remind you of the (unfortunately) pessimistic comments I expressed in these chronicles both before and after the last COP summit held in Egypt in 2022. I referred to the presence on site and the interference of pro-fossil fuel lobbies and politicians. The next summit, which will be chaired by Sultan Al-Jaber, United Arab Emirates Energy Minister and chairman of Abu Dhabi's national oil company, is rather akin to a global public health convention on tobacco control being held at the headquarters of a cigarette company and chaired by its CEO.

We wish you a pleasant read!

# THE ENVIRONMENTAL AND SOCIAL COSTS OF AI STIR DFBATF

A song featuring Drake created entirely by Artificial Intelligence (AI) could win a Grammy Award. An image crafted by AI won first prize in the Creative Category of this year's Sony World Photography Award. The pope was seen flaunt-

ing a designer white puffer jacket... These visible effects of artificial intelligence are raising multiple social, environmental. and ethical issues.

#### SOCIAL IMPACT

The recent breakthroughs made by AI technologies such as ChatGPT could have significant implications for the job market and the distribution of work in the future. As AI becomes increasingly reliable and effective, many of the tasks that had been carried out by humans until today are likely to become automated. This could potentially lead to job

losses in several industries, notably those involving routine or repetitive tasks. According to McKinsey, AI could improve a company's efficiency by over 40% and reduce its operating costs by up to 30%.

But AI can also create new jobs in the development, maintenance, and supervision of the AI systems themselves. Faced with these new technologies, companies will have to adapt by re-skilling and upskilling their employees. A new study by the International Labour Organization (ILO) has corroborated this observation, while also warning that the potential effects of generative AI are likely to differ greatly between men and women. The impact of automation on jobs traditionally held by women could be up to twice as high.

### ENVIRONMENTAL IMPACT

The impact of AI on the environment is rather complex: the lack of transparency and diversity of uses are not compatible with the calculation of accurate carbon footprints; yet the data centers used to train and use the models require large amounts of electricity and water for their cooling systems.

Nevertheless, AI can also have positive impacts. One example is weather prediction, where technology can

> forecast the production of power from wind farms, or forest fires. Climate Q&A is also a free chatbot that answers questions on climate issues, drawing from the IPCC report, for instance. Other observers fear excess consumer spending patterns induced by the ever-more targeted and effective advertising enabled by AI.

#### SOCIETAL IMPACT

Issues around security, the protection of privacy and the fight against cyberattacks will become increasingly acute. However, the key issues today are the safeguards needed to counter ethical or legal drifts caused by an uncontrolled use of AI. What happens when generative AI exploits copyrighted material? How

can we guarantee that fake information will not be disseminated? And how can the discrimination generated by a biased AI be prevented?

The consequence is that regulation will flourish. In May this year, leaders of the G7 countries announced the creation of a taskforce on artificial intelligence to discuss a "responsible use" of these tools and the risks their carry, including the risk of "disinformation".

The European law on AI should help to contain the risks that have already been identified, by setting a list of banned practices and high-risk systems, as well as legal requirements - including, for example, imposing that companies publish the sources they use.

The authors of the above-mentioned study have pointed out that "the results generated by the technological transition are not pre-determined. The decision to incorporate these technologies was made by humans; and humans will have to guide the transition process".



# FAMILY FIRMS AND CARBON EMISSIONS

#### MARCIN BORSUK

Marcin Borsuk is an Assistant Professor at the Institute of Economics of the Polish Academy of Sciences, a researcher at the University of Cape Town, and a Financial Stability Expert at the National Bank of Poland. His primary research interests lie in the areas of financial stability, financial intermediation, and climate-related financial risks.

#### NICOLAS EUGSTER

Nicolas Eugster is a Lecturer in finance at The University of Queensland School of Business. He was previously an Assistant Professor at the IESEG School of Management and a visiting scholar at the University of Maryland. Nicolas' research interests focus on corporate finance, corporate governance, ownership structure, and family firms.

#### PAUL-OLIVIER KLEIN

Paul-Olivier Klein is an Assistant Professor in Finance at the University of Lyon, France. His research interests cover corporate governance, financial stability, and Islamic finance.

#### OSKAR KOWALEWSKI

Oskar Kowalewski is Professor of finance at the IESEG School of Management, member of LEM-CNRS 9221 and the Institute of Economics, Polish Academy of Science. His main research interests are in the areas of banking, corporate finance, and corporate governance, and recently agroeconomics. While concerns about climate change continue to escalate on a global scale, the significant impact of carbon dioxide emissions  $(CO_2)$  on the climate not only poses a serious threat to human habitability but also has implications for the stability of global economies. Market players, who are becoming increasingly aware of the environmental consequences and financial risks associated with climate change, are progressively adopting measures to integrate environmental sustainability into their business strategies. However, it's essential to recognize that the approach to environmental responsibility isn't uniform across all companies. This diversity in environmental commitment is especially pronounced in family firms, which are recognized for their involvement in environmental stewardship. The present study, published in 2023, offers profound insights into the intricate relationship between family firms and carbon emissions.

### STUDY APPROACH

There is no unique definition of a family firm, so the authors of this study define firms as "family-owned" if the founder or a member of the founding family is an officer, director or owns more than 5% of the firm's equity, individually or as a group. Employing a substantial cross-country dataset comprising 6,610 non-financial companies spanning the years 2010-2019, this dataset encompasses a wide range of industries and geographic regions, providing a robust foundation for rigorous analysis. To quantify CO<sub>2</sub> emissions, the study relies on comprehensive, globally sourced emissions data that measure the amount of CO<sub>2</sub> released by each company. These emissions are evaluated through two critical dimensions: emissions intensity and absolute emissions. Emissions intensity represents the amount of CO<sub>2</sub> produced per unit of economic output, offering a measure of a company's carbon footprint efficiency in its productivity. Conversely, absolute emissions provide an overview of the total volume of CO<sub>2</sub> emissions generated by a company, offering a comprehensive perspective on its environmental impact. Using these emissions metrics, the study examines whether the environmental performance of family-owned businesses outstrips that of non-family-owned businesses in various sectors and regions.

## THE INFLUENCE OF FAMILY VALUES ON ENVIRONMENTAL PRACTICES

Based on empirical research, one of the primary factors that drives family firms to adopt strategies for reducing carbon emissions is their recognition of the potential financial advantages associated with pollution reduction. This motivation aligns with the wider corporate landscape, where firms, regardless of ownership type, share a common drive for financial benefits when implementing environmental strategies. Family firms, in particular, often embrace a long-term perspective, influenced by their desire to pass the firm down to the next generation. Their commitment to safeguarding their family legacy and preserving their identity serves as a powerful incentive to reduce greenhouse gas emissions, ensuring the long-term viability of their firm. This long-term outlook reduces the discount factor applied to their investment horizon, making immediate pollution reduction more attractive. Moreover, family firms frequently exhibit a higher degree of risk aversion, which can be attributed to their concentrated portfolio holdings. As such. they are more aware of the potential negative impacts of climate change on their operations, making them more inclined to adopt bold and proactive measures to address and mitigate the effects of climate change. Additionally, family firms place a significant emphasis on reputational expenses, thereby rendering them

more susceptible to diverse institutional constraints, such as government regulations, apprehensions regarding media exposure, and conprevailing formity with social norms. This elevated awareness of the potential hazards associated with their reputation may prompt family firms to voluntarily adopt environmentally responsible practices that transcend mere compliance with regulatory mandates and industry standards

### **KEY FINDINGS**

The comprehensive study's principal findings reveal significant distinctions between family firms and their non-family counterparts in terms of CO<sub>2</sub> emissions. Family firms exhibit notably lower CO<sub>2</sub> emissions, encompassing both direct and indirect emissions, even after meticulous control for various firm-specific factors, country, industry, and year fixed effects. This discrepancy underscores family ownership's profound dedication to environmental protection. Intriguingly, the advantageous impact of family ownership on CO<sub>2</sub> emissions is primarily concentrated within specific sectors: Consumption of Goods, Health Care, and Oil and Gas. This environmental conscientiousness is also more pronounced in North America.

FAMILY FIRMS, IN PARTICULAR. OFTEN EMBRACF A LONG-TERM PERSPECTIVE. INFLUENCED BY THEIR DESIRE TO PASS THE FIRM DOWN TO THE NEXT GENERATION. THEIR COMMITMENT TO SAFEGUARDING THEIR FAMILY LEGACY AND PRESERVING THEIR **IDENTITY SERVES** AS A POWERFUL **INCENTIVE** TO REDUCE GREENHOUSE GAS EMISSIONS. ENSURING THE LONG-TERM VIABILITY OF THEIR FIRM.

with additional reductions in emissions, highlighting the importance of family firms' long-term vision. Additionally, family-oriented firms, where family members are more involved in management and governance, tend to have lower emissions. Family firms also

> increased their investment in research and development after the 2015 Paris Agreement. This suggests that some of the observed reductions in emissions are linked to innovations and technical changes in their production or service processes. Finally, despite polluting less, family firms are more reluctant to publicly commit to reducing their greenhouse gas emissions and consequently obtain lower Environmental, Social, and Governance (ESG) scores compared to non-family firms. This paradox suggests that family firms have a lower propensity for "greenwashing".

> This study highlights a significant influence of ownership type on environmental performance, even if companies themselves may not be fully cognizant of this impact, as evidenced by their subdued public commitments and lower ESG environmental scores. This effect may be attributed to the governance mechanisms and values instilled by diverse ownership models. Considering the threats posed by global warming and climate change over the coming decades, it is imperative to further investigate how ownership structure influences firms' non-financial motivations

## POTENTIAL CATALYSTS

The study explores a number potential catalysts that might explain the results. An analysis following the 2015 Paris Agreement reveals that family firms exhibited a greater reduction in emissions intensity after this landmark event. This suggests that family firms became more environmentally conscious and responsive to global sustainability initiatives following the agreement. Relating to governance aspects, longer board tenure in family firms is associated and, subsequently, their environmental footprint. This could potentially pave the way for the implementation of public policies that take into account these effects. Policies should be based on actual pollution metrics rather than firms' commitments and communication, given the significant disparity between them.

Borsuk M., Eugster N., Klein P-O., Kowalewski O., Family Firms and Carbon Emissions (latest version), Available at SSRN: https://ssrn.com/abstract=4405296 or http://dx.doi.org/10.2139/ssrn.4405296 (version March 30, 2023).

#### RECOMMENDED READING

# EDP RENOVAVEIS: RENEWABLE ENERGY IS CORE TO THE TRANSITION



EDP Renovaveis (EDPR), 75% owned by its Portuguese mother-company EDP, specialises in the production of electricity from renewable sources, with a global portfolio of 14.7 GW at the end of 2022, up 10% since 2021.

While the vast majority of its assets are located in Europe (38%) and North America (49%), EDPR is also turning to Asia – with the acquisition of Sunseap and the integration of 2.1 GW, mainly in the APAC region. The company produces electricity from onshore wind farms (86%), solar energy (11%) and offshore wind farms (2%).

The 25-billion-euro investment plan over 2023-2026 will support the group's objective to achieve net zero by 2040. The group's strategy is to double its installed capacity and add 20 GW by the end of 2025. Interestingly, EDPR is one of the few companies in Europe with both revenue and capex 100% aligned with the EU's Green Taxonomy. On social aspects, the group invests in staff training (98% of employees benefited from a least one training course in 2022) and has built a preventative health & safety culture (EDPR aims for zero accident). Finally, in 2021, EDP & EDPR reacted swiftly and renewed their executive teams, including the Chairman, following a case of corruption involving two former senior executives.

The information about the companies cannot be assimilated to an opinion of Edmond de Rothschild Asset Management (France) on the expected evolution of the securities and on the foreseeable evolution of the price of the financial instruments they issue. This information cannot be interpreted as a recommendation to buy or sell such securities.

# A WORLD WITHOUT WORK?

Daniel Susskind is a Research Professor in Economics at Oxford University and King's College in London. In his thought-provoking book, he explores the future of work in the age of new technologies and artificial intelligence (AI), looking beyond purely economic aspects and raising multiple, open-ended challenges. For anyone interested in these topics, this is the book to read. What will be the pace of automation? What about substitution or complementarity at work? Is Al like other new technologies? Will there be enough well-paid work to go round? Are we heading towards a leisure-driven society? What about access to the new skills required? What role can governments play? How should we feel about the growing power of US and Chinese tech giants? And how can we limit rising inequalities ?



A World Without Work by Daniel Susskind

# 40% of the 500

companies and financial institutions targeted by Forest 500 have not yet defined a policy to combat deforestation. Forest 500 identifies the 350 companies and 150 financial institutions most at risk from tropical deforestation and assesses them each year on the strength and implementation of their commitments on deforestation and human rights.

Source: Forest 500. Data as of February 2023.

60.6%

of the world's population is on social networks.

Source: We are Social, Hootsuite, Blog du Modérateur, Digimind, Statista. Data to end July 2023.

# EDMOND DE ROTHSCHILD ASSET MANAGEMENT (FRANCE) HAS JOINED THE "NATURE ACTION 100" INITIATIVE AS A FOUNDING MEMBER

#### 2023 was a milestone for Edmond de Rothschild's global ESG strategy as the firm considerably reinforced its existing pledge to support the energy and environmental transition.

After joining the Institutional Investors Group on Climate Change (IIGCC) and the Net Zero Asset Managers (NZAM) in the first half of 2023, reaffirming our commitment to achieve "net zero greenhouse gas emissions by 2050", and consistent with the efforts deployed internationally to limit global warming to 1.5°C, Edmond de Rothschild Asset Management (France) became a founding member of the "Nature Action 100" initiative.

The project was initiated in December 2022 during a side-session of the COP 15 in Montréal. Its effective launch took place on September 26th of this year. Nature Action 100 is backed by the Ceres and the IIGCC, with the Finance for Biodiversity Foundation and Planet Tracker co-leading the Technical Advisory Group.

## PRESERVING NATURE AND BIODIVERSITY

This global investor engagement initiative mobilizes institutional investors to drive greater corporate ambition and action to stem nature and biodiversity loss. The initiative will target companies with strong dependencies on nature, or that are large drivers of nature loss globally, initially focusing on 8 sectors: biotechnology and pharmaceuticals; chemicals; household goods; consumer goods retail; food, ranging from meat and dairy producers to processed foods; food and beverage retail; forestry and packaging, including forest management and pulp and paper products; and metals and mining.

Specifically, the initiative:

- Maps sector pathways for driving greater corporate ambition and action on nature.
- Coordinates, informs, and supports engagements between investors and company executives and board members.
- Details ambitious actions that need to be undertaken by companies to protect and restore nature.
- Tracks the progress of companies against key benchmark indicators and provides annual progress.

This new commitment builds on our existing approach based on active and focused shareholder dialogue. It is also consistent with our ambition to achieve carbon neutrality for all our assets under management by 2050.

Let us not forget that climate change is one of the main direct drivers of biodiversity loss.

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#### EDMOND DE ROTHSCHILD ASSET MANAGEMENT (FRANCE)

47, rue du Faubourg Saint-Honoré, 75401 Paris Cedex 08

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