System Change Investing – The Business Case

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System Change Investing (SCI) provides a significant opportunity for investment companies to increase assets under management, enhance investment returns and position themselves as global leaders in the rapidly growing $30 trillion Sustainable/Responsible Investing (SRI) market. The new paradigm approach shifts the focus of investing from company change and symptoms to system change and root causes. This enables SCI to provide the highest possible sustainability benefits and capture a substantial share of the SRI market.

Over the past 20 years, SRI and corporate sustainability have become mainstream. Nearly all large companies and financial institutions have implemented sustainability strategies. The main driver of this is the growing financial relevance of environmental and social issues. Companies are not separate from the larger environmental and social systems that contain and sustain them. As the human population and economy expand in the finite Earth system, negative corporate impacts return more quickly to harm companies, often in the form of market rejection, lawsuits and reputation damage. Companies have increasingly strong financial incentives to reduce negative environmental and social impacts.

Several additional factors are driving rapid SRI market growth. These include increasing regulations, rising pension fund SRI requirements, high market growth of sustainable products, large financial and competitive benefits of corporate sustainability strategies, superior SRI fund returns, and expanding public concerns about environmental and social conditions. Widespread youth demonstrations against climate change show rising public unwillingness to tolerate negative corporate environmental and social impacts.

SRI and corporate sustainability provide substantial benefits. But in spite of this good work, every major environmental life support system is in rapid decline, with some regional exceptions. Inequality and many other social problems are growing rapidly. Businesses cause extensive environmental and social degradation. This situation is increasingly untenable. It creates rapidly growing problems for companies, investors and society.

System Change

New investment and corporate sustainability approaches are needed to reverse environmental and social degradation and achieve the UN Sustainable Development Goals (SDGs). Economic and political systems were developed from a reductionistic perspective that does not adequately address many relevant factors, such as the negative environmental and social impacts of economic activity. Through many specific system flaws (i.e. externalities, time value of money, limited liability), these myopic systems do not hold companies fully responsible for negative impacts. This makes it impossible to fully eliminate impacts in competitive markets.

Very generally speaking, businesses can mitigate about 20 percent of short-term and long-term, tangible and intangible, negative environmental and social impacts in a profit-neutral or profit-enhancing manner. Beyond this point, costs usually increase. If companies continue impact reduction, they will put themselves out of business long before reaching full impact mitigation.

Myopic systems put businesses in conflict with society and humanity in conflict with nature. These systems unintentionally compel all companies, without exception, to degrade the environment and society. They are the root causes of the environmental, social and economic problems addressed by the SDGs. System change is at least 80 percent of the sustainability/SDG solution. But it gets relatively little attention in the investment area.

Nearly all SRI funds, corporate sustainability strategies and SDG efforts are focused on addressing symptoms (environmental, social, economic problems) and encouraging companies to voluntarily reduce negative impacts. This will not work. Addressing symptoms instead of root causes is like trying to put out a fire while simultaneously throwing gasoline on it.

System Change Investing

SRI successfully encouraged companies to implement sustainability strategies. The same proven approach can be used to engage the corporate and financial sectors in system change. SCI involves rating companies on system change performance, and then using the ratings to develop investment funds.

The first SCI rating model (Total Corporate Responsibility – TCR®) was developed in 2003. TCR is segregated into three broad areas – traditional ESG, mid-level system change (sector, stakeholder, environmental/social issue-level) and high-level system change (economic, political, social system-level). Examples of SCI metric categories include system change strategies, public awareness and media campaigns, system change collaboration, government influence activities, addressing specific system flaws, and supporting NGOs, academia and other groups that are promoting system change.

SCI ratings assess systemic risks and opportunities and provide strong indicators of management quality and stock market potential. They can be used as overlays to enhance the financial returns of value, growth, index and many other types of investment funds. SCI is focused on the most important sustainability issue – system change. As a result, SCI funds can provide far greater sustainability benefits than any other type of SRI. Financial institutions launching SCI funds will be seen as the true sustainability and SRI leaders.

Systemic changes are needed in all areas of society to achieve sustainability and the SDGs, including government, general public and corporate/financial. Vested interest controlled governments are unlikely to change on their own. Empowering citizens to work together on their many common interests is a longer-term issue. Engaging the corporate and financial sectors is the most powerful short-term system change strategy.

System change is the most important and complex challenge facing humanity. We do not need to fully understand how to evolve systems before beginning. The key issue in the business area is to send the system change signal from investors to companies. Once investors shift investments based on system change performance, companies will implement collaborative system change strategies. Effective system change protects business and society. It makes acting in a fully responsible manner the profit-maximizing strategy.

Climate change illustrates the importance of system change. The root cause of climate change is not greenhouse gas emissions. It is the flawed economic and political systems that compel companies to emit these gases, for example, by heavily subsidizing fossil fuels and not holding companies fully responsible for harmful emissions.

System change is highly efficient. The environmental, social and economic problems addressed by the SDGs have a common root cause – reductionistic thinking and resulting flawed systems. Therefore, they have a common solution – using whole system thinking to evolve systems into sustainable forms.

System change not only is the most important action required to halt global warming. It also is the most important strategy needed to resolve virtually every other major challenge facing humanity. Investment companies launching SCI funds can gain first mover advantage and forever be seen as pioneers of the most important action needed to achieve the SDGs and protect business and society.

This article briefly summarizes the SCI business case and implementation mechanics. Far more detailed descriptions are provided in the many articles on www.GlobalSystemChange.com and in the Global System Change books.

Frank Dixon established Global System Change in 2005. He recognized that system change would become the dominant sustainability issue of the 21st Century. His experience as the Managing Director of Research for the largest ESG research company (Innovest) and sustainability advisor to Walmart and other organizations showed that flawed economic and political systems compel all companies to degrade the environment and society. He conducted several years of multidisciplinary research to produce a true whole system approach to sustainability (described in the Global System Change books). The approach provides practical system change strategies for all major areas of society. In the corporate and financial sectors, System Change Investing represents the most advanced and effective sustainability strategy. Frank Dixon advises businesses, investors and governments on sustainability and system change. He has presented at many corporate and financial sector conferences around the world, as well as leading universities, including Harvard, Yale, Stanford, MIT and Cambridge. Frank Dixon is an Associate Fellow of the World Academy of Art and Science. He has an MBA from the Harvard Business School.

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